Corporate governance and business ethics

Stefy m m
Dept of commerce
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COMMITTEES ON CORPORATE GOVERNANCE

THE BLUE RIBBON COMMITTEE

The Blue Ribbon Committee was jointly sponsored by the **New York Stock Exchange (NYSE) & National Association of Security Dealers(NASD)** for improving the working of corporate Audit Committee.

RECOMMENDATIONS OF BLUE RIBBON COMMITTEE

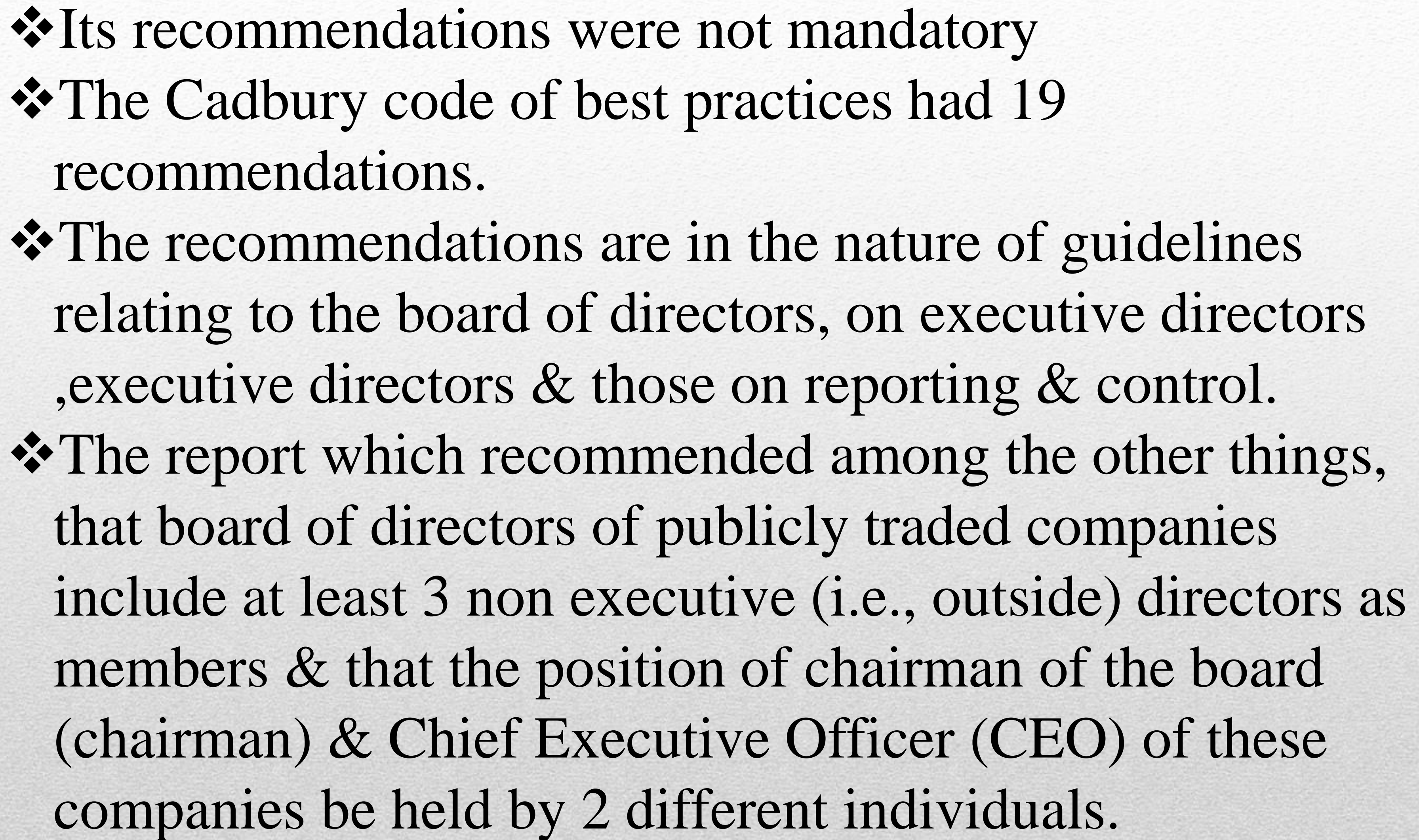
The committee has given certain recommendations specifically for the Audit Committees. These Recommendations are;

- The members of the committee should be independent directors & financial literate.
- External auditors being the representatives of shareholders should periodically discuss the quality of company's accounting principles in relation to General Accepted Accounting Principles(GAAP) with the audit committee.

- Statutory auditors should maintain their independence in discharging their professional responsibilities.
- On annual basis, the committee should review & discuss with the accountants. Blue Ribbon Committee has also recommended that Audit committee should have formal written character.

THE CADBURY COMMITTEE

- The Cadbury committee was appointed by the Government of the United Kingdom(UK) in May 1991 with a board mandate to "address the financial aspects of corporate governance".
- The committee investigated the accountability of the board of directors to shareholders & to society.
- It submitted its report & associated "code of best practices "in 1992 where in it provides the method of governance needed to achieve a balance between the essential power of the board of directors & their accountability.


❖Its recommendations were not mandatory
❖The Cadbury code of best practices had 19 recommendations.
❖The recommendations are in the nature of guidelines relating to the board of directors, on executive directors ,executive directors & those on reporting & control.
❖The report which recommended among the other things, that board of directors of publicly traded companies include at least 3 non executive (i.e., outside) directors as members & that the position of chairman of the board (chairman) & Chief Executive Officer (CEO) of these companies be held by 2 different individuals.

Its important recommendations include the setting up of on audit committee with independent members.

1. The board should include non executive directors of sufficient caliber & number for their views to carry significant weight in the board's decisions.
2. The board should have a formal schedule of matters specifically reserved to it for decisions to ensure that the direction & control of the company is firmly in its hands.
3. There should be an agreed procedure for directors in the furtherance of their duties to take independent professional advice if necessary, at the company's expense.
4. All directors should have access to the advise & services of the company secretary.

THE GREENBURY COMMITTEE (1995)

During the 1990's the issue of directors remuneration was becoming a primary concern for investors & the public at large. Consequently ,it was recognized that corporate governance issues relating to directors remuneration needed to addressed in a more careful manner. This lead to the establishment of the Greenbury Committee.

- The Greenbury Committee was set up in january,1995.
- It established to identify the good practices by the Confederation of British Industry(CBI), in determining directors remuneration & to prepare a code of such practices for use by public Ltd. Companies of United Kingdom.

The Committee’s finding were documented in the Greenbury Report ,which incorporated a Code of Best Practices on Director’s Remuneration.

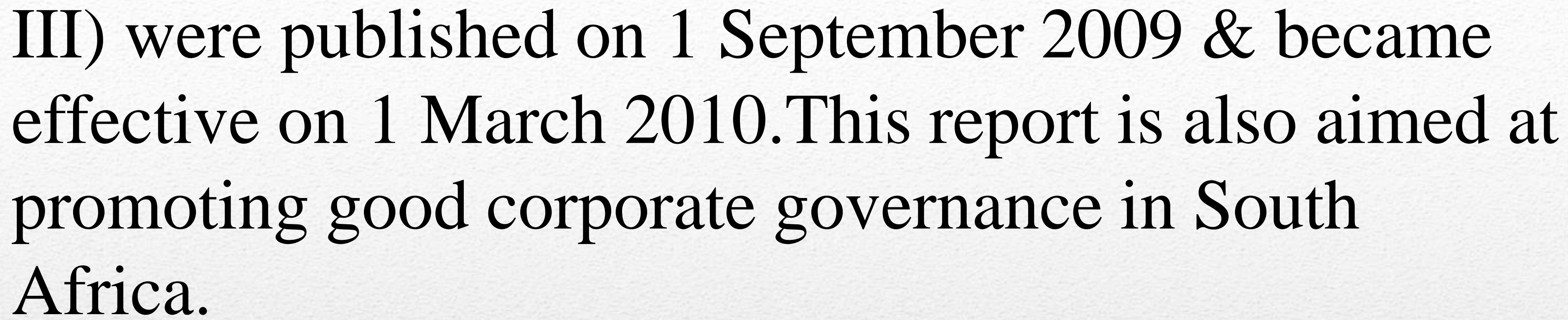
Specifically 4 main issues were dealt with as follows;

1. **Remuneration committee**: The role of Remuneration Committee in setting the remuneration packages for the CEO & other directors.
2. **Disclosures**: The required level of disclosure needed by shareholders regarding details of directors remuneration & whether there is need to obtain shareholders approval.
3. **Remuneration Policy**: Specific guidelines for determining a remuneration policy for directors &
4. **Services Contracts & Compensation**: Service contracts & provision binding the company to pay compensations to directors.

Kings Committee

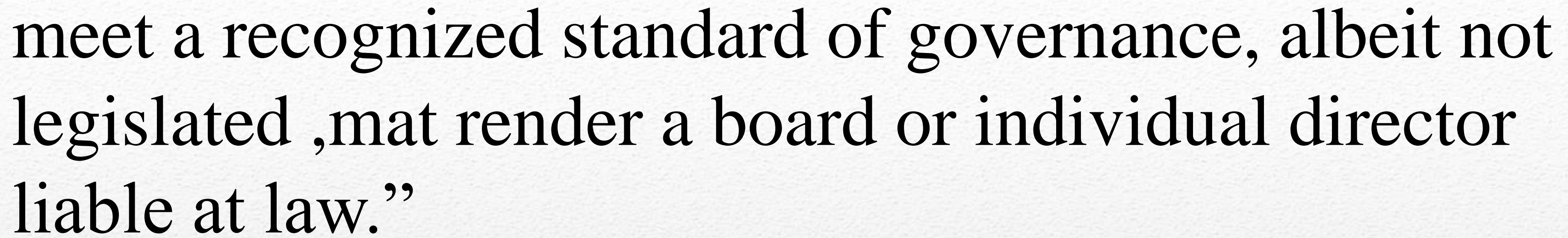
- King committee was constituted under the chairmanship of Professor Mervyn E. King in 1992.
- With Specific aim of researching & making recommendations into corporate governance in South Africa.
- The King committee has received both local & international reputation for its contribution towards corporate governance.

- ***King 1 Report***: It was published in 1994 & recognized that companies do not act independent from society. For this reason the highest standards of corporate governance were encouraged through enterprise with integrity.
- ***King II Report:*** It was released in 2002.King II was more focused on introducing the idea of corporate citizenship & the notion of the triple bottom line. Some of the recommended practices of king II report was incorporated into the companies Act 71 of 2008 & some have become regulatory prescriptions to companies listed on the Johannesburg Stock Exchange.
- ***King III Report:*** The King Code of Governance Principals & the King Report on Governance for South Africa (King


III) were published on 1 September 2009 & became effective on 1 March 2010.This report is also aimed at promoting good corporate governance in South Africa.

King III now states that “Good governance is not something that exists separate from the law & it is inappropriate to unhinge governance from the law.”

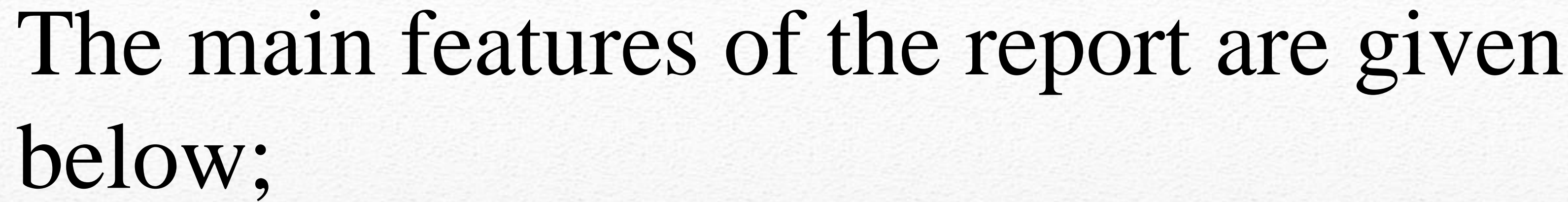
King III further argues that “Corporate governance & practices, codes & guidelines therefore lift the bar of what are regarded as appropriate standards of conduct. Consequently, any failure to



meet a recognized standard of governance, albeit not legislated ,mat render a board or individual director liable at law.”

The King committee was noticeably more concerned with the governance of commercial companies.

- ***King IV Report***: ‘Transparency’ is the basis of King IV report. With the introduction of an ‘apply & explain’ regime, King IV asks organizations to be transparent in the application of their corporate governance practices.



The main features of the report are given below;

1) A set of voluntary principles & leading practices.
2) Applicable to all organisations, regardless of their form of incorporation.
3) It focuses on outcomes.
4) The code differentiates between principles & practices.
5) Apply & explain regime.

THE HAMPEL COMMITTEE,1996

- The Hampel committee was established in1996.
- Established to review & revise the earlier recommendations of cadbury & greenbury committee.
- Its aim was to promote high standards on corporate governance both to protect investors & preserve enhance the standing of companies listed on the London Stock Exchange.
- The report emphasized principles of good governance rather than explicit rules in order to reduce the

regulatory burden on companies.

- Hampel viewed governance from a strict principal/agent perspective regarding corporate governance as an opportunity to enhance long term shareholder value.
- Another key advance was in the area of accountability & audit.

The committee developed further the Cadbury report & it maid the following recommendations;

1) The auditors should report on the internal control privately to the directors
2) The directors maintain & review all controls
3) Companies should time to time review rather their need for internal audit function & control.

THE COMBINED CODE ,1998

The Combined Code was subsequently derived from Ron Hampel Committee's Final Report, Cadbury &the Greenbury Report.

1. The board should maintain a sound system of internal control to safeguard shareholders investment & the companies assets.
2. It was observed by this committee that the one common denominator behind the past failures in the corporate world was the lack of effective risk management.

THE TURNBULL COMMITTEE ,1999

- The Turnbull committee was set by The Institute of Chartered Accountant in England & Wales(ICAEW) in 1999.
- It set up to provide guidance to assist companies in implementing the requirements of the Combined Code relating to internal control.

Recommendations;

1. Where companies do not have any internal audit function; the board should consider the need for carrying out an internal audit function.
2. The board of directors should confirm the existence of procedures for evaluating & managing the key risks.

SARBANES-OXLEY ACT,2002

- The Sarbanes-Oxley Act(SOXACT), 2002 is a sincere attempt to address all the issues associated with corporate failures to achieve quality governance & to restore investor's confidence.
- The Act was formulated to protect investors by improving the accuracy & reliability of corporate disclosures, made precious to the securities laws & for other purposes.

INDIAN COMMITTEES

Confederation of Indian Industry(CII) ,the Association Chamber of Commerce & Industry (ASSOCHAM) & the Securities & Exchange Board of India(SEBI) constituted committees to recommend initiatives in Corporate Governance. Some major committees for corporate governance in India are:

1. Kumar Mangalam Birla Committee,1999
2. Narayan Murthy Committee Report,2003
3. Dr.J.J Irani committee on company Law,2005
4. Naresh Chandra Committee Report,2002
5. Uday Kotak Committee Report,2017

KUMAR MANGALAM BIRLA COMMITTEE,1999

- ◊ The Securities & Exchange Board of India (SEBI) which set up the committee under the chairmanship of Kumar Mangalam Birla in1999.
- ◊ Objective is to promote & raising standards of good corporate governance.
- ◊ The primary objective of the committee was to view corporate governance from the perspective of the investors & shareholders & to prepare a Code to suit the Indian corporate environment.
- ◊ In early 2000 the SEBI Board accepted & ratified the key recommendations of this committee & these were incorporated into Clause-49 of the Listing Agreement of the Stock Exchanges.
- ◊ The committee divided the recommendation into 2 categories ,namely mandatory & non-mandatory.

Mandatory Recommendations

1. Applies to listed companies with paid-up capital of Rs.3crore & above.
2. Composition of board of directors-optimum contribution of executive & non executive directors.
3. Audit committee with independent directors with one having financial & accounting knowledge.
4. Remuneration committee.
5. Board procedures-at least 4 meetings of board in a year with maximum gap of 4 month between 2 meeting. Directors shall not be a member of more than 10 committees & shall not act as chairman of more than 5 committees across all companies.
6. Management decision & analyzing report covering industry structure, opportunities, threats, risks, outlook & internal control system.
7. Information sharing with shareholders.

Non-Mandatory Recommendations

1. Role of chairman
2. Remuneration committee of board.
3. Shareholders right for receiving half yearly financial performance postal ballot covering critical matters like alteration in memorandum etc.
4. Sale of whole or substantial part of the undertaking.
5. Corporate restructuring.
6. Further issue of capital.
7. Venturing into a new businesses.

NARAYANA MURTHY COMMITTEE REPORT,2003

- SEBI constituted theh committee under the chair man ship of Shri N.R. Narayana Murthy, Chairman & Chief Mentor of Infosys Technology Ltd.
- It was established to evaluate the adequacy of existing corporate governance practices 7 future improvement of these practices.
- It was setup to review clause 49 & suggest , measures to improve corporate governance standards.
- The Committee comprises members from various walks of public & professional life.

The Committee's terms of the References were to:

i. Review the performance of corporate governance;&
ii. Determine the role of companies in responding to rumour & price sensitive information circulating in the market in order to enhance the transparency & integrity of the market.

- Some of the major recommendations of the committee primarily related to audit committees, audit reports, independent directors, related party transactions, risk management, directorships & director compensation , codes of conduct & financial disclosures.

Mandatory Recommendations

1. Strengthening the responsibilities of audit committees.
2. Improving the quality of financial disclosures, including those related to party transactions & proceeds from initial public offerings.
3. Requiring corporate executives boards to assess & disclose business risks.
4. The annual reports of companies; introducing responsibilities on board to adopt formal codes of conduct.
5. The position of nominee directors& stock holder approval & improved disclosures relating to compensation paid to non-executive directors.

Non-Mandatory recommendations

1. Moving to regime where corporate financial statements are not qualified.
2. Instituting a system of training of board members &
3. Evaluation of performance of board members.

DR. J.J IRANI COMMITTEE REPORT

- ♣ Ministry of Corporate Affairs began the review & redrafting of the Companies Act 1956.
- ♣ The government therefore took a fresh initiative in this regard & constituted a committee in December 2004 under the Chairmanship of Dr.J.J Irani with task of advising government on the proposed revisions to the companies Act 1956.
- ♣ The recommendations of the committee submitted in May 2005.
- ♣ Based on the recommendations ,the Companies Bill (2008)was introduced in Parliament. But the bill lapsed due to dissolution of the Lok Sabha.
- ♣ It was reintroduced in 2009 & 2011 but was also withdrawn by the government.
- ♣ A revised bill was introduced in Parliament in 2012 & approved on 29th August 2013.
- ♣ A new companies Act (2013) came into force with effect from 30th August 2013.

The main features of its recommendations pertaining to corporate governance are as follows;

- Number of Directors & their duration in company.
- Age of Directors
- 1/3rd of Independent Directors
- Maximum No.of Directorship hold by individual
- Remuneration policy
- Sitting Fee Structure for Directors
- Requisite Board Meeting in a year
- Number of Independent Directors in Audit Committee
- Constitution of Remuneration Committee
- Protection of minority shareholders rights
- Appointment of Auditors
- Certificate Issued by CEO & CFO
- Appointment of Nominee Directors
- Whistle-blower concept
- Subsidiary company transaction
- Appointment of Stakeholders Relationship committee

Chairman & CEO Duality (particularly in regard to separation of these 2 posts) & Appointment of Nomination Committee.

NARESHCHANDRA COMMITTEE REPORT ,2002

- The Naresh Chandra Committee was appointed as a high-level committee to examine various corporate governance issues by the Department of Company Affairs on 21 August 2002.
- Naresh Chandra Committee report on Corporate Audit &Governance has taken forward the recommendations of Kumar Mangalam Birla Committee on corporate governance which was set up by the securities Exchange Board of India on the following counts:

a. Representation of independent directors on a company’s board
b. The composition of audit committee.

Recommendations

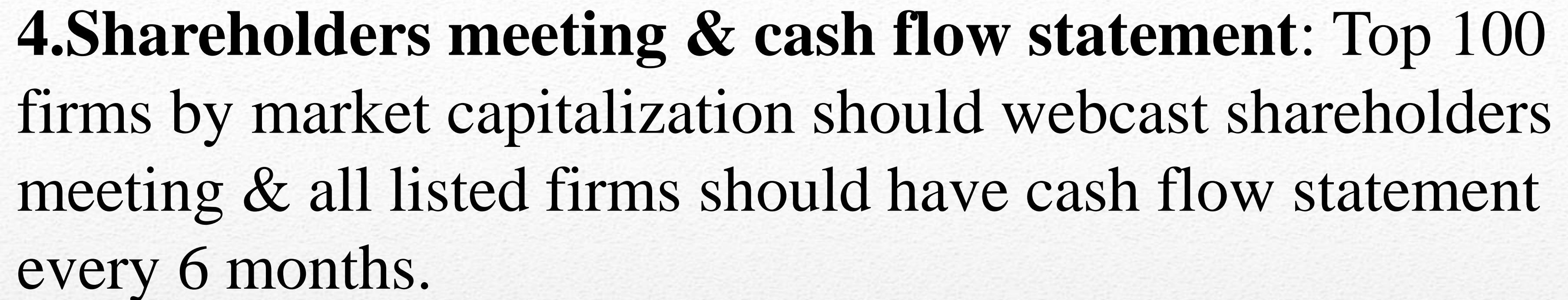
1. Tightening of the control around auditors by asking them to make many disclosures.
2. Calling upon CEOs &CFOs of all listing companies to certify their companies annual accounts, besides suggesting.
3. Setting up of quality review boards by the Institute of Chartered Accountants of India (ICAI),Institute of Company Secretaries of India(ICSI) & Institute of Cost & Works Accountants of India, instead of a Public oversight board similar to the one in USA.

UDAY KOTAK COMMITTEE REPORT,2017

- The Uday Kotak committee was constituted by SEBI in June 2017.
- 21 member committee on corporate governance headed by banker Uday Kotak has submitted its report to the SEBI.
- Its primary objective was improving standards concerning corporate governance of listed companies in India.

The committee submitted its report detailing several recommendations on October 5,2017.

1. **Separation of the roles**: Roles of chairman & managing director at listed firms should be separated & chairman ship should be limited to only non executive directors.
2. **Minimum board strength**: It should be increased to 6 members & at least 1 woman should be appointed as independent director. At least 5 board meeting for listed firms should be held in year up from current practice of 4 meetings.
3. **Independent Directors**: At least half of board members to be independent directors at listed companies, while all directors must attend at least half of board meeting.



4.Shareholders meeting & cash flow statement: Top 100 firms by market capitalization should webcast shareholders meeting & all listed firms should have cash flow statement every 6 months.

5. Credit ratings: Updated list of all credit ratings obtained by the listed entity must be made available at one place , which would be very helpful for investors & other stakeholders.

6.Minimum remuneration: Independent directors must get minimum remuneration of Rs.5 lakh p.a & sitting fee of 20,000-50,000 for each board meeting.

7.Risk management &IT committee: Top 500 listed companies should have risk management committee of boards for cyber security.

CORPORATE REPORTING FRAMEWORK

- ♠ The term reporting frame work is defined as a set of criteria used to determine measurement, recognition, presentation & disclosure of all material information in reports.
- ♠ A key component in corporate reporting is an annual corporate report.
- ♠ It is a comprehensive report intended to give information to shareholders & other interested people about a company’s activities & financial performance throughout the preceding year.

An annual report will include the following:

a. Chairman's report
b. CEO’s report
c. Auditors report on corporate governance
d. Mission statement
e. Corporate governance statement compliance
f. Statement of directors responsibilities
g. Invitation to the company’s AGM

a. Auditor’s report on financial statements
b. Balance sheet
c. Statement of retained earnings
d. Income statement
e. Cash flow statement
f. Notes to the financial statements
g. Accounting policies

Every listed companies shall disclose in the Board's report the following ;

i. The ratio of the remuneration of each director to the median employee's remuneration & such other details as may be prescribed.
ii. The percentage increase in remuneration of each director, chief financial officer, Chief Executive Officer, Company Secretary or Manager, if any ,in the financial year.
iii. The percentage increase in the median remuneration of employees in the financial year.
iv. The no.of permanent employees on the rolls of company.
v. Average percentile increase already made in the salaries of employees other than managerial personnel in the last financial year & its comparison with the percentile increase in the managerial remuneration & justification there of & point out if there are any exceptional circumstances for increase in the managerial remuneration
vi. The key parameter for any variable component of remuneration availed by the directors.
vii. Affirmation that the remuneration is as per the remuneration policy of the company.

Remuneration

The following disclosures on the remuneration of directors shall be made in the section on the corporate governance of the annual report.

a) All elements of remuneration package of all directors i.e. salary ,benefits, bonuses, stock options, pension etc.

b) Details of fixed component & performance linked incentives, along with the performance criteria.

c) Service contracts, notice period, severance fees.

d) Stock option details, if any - & whether issued at a discount as well as the period over which accrued & over which exercisable.

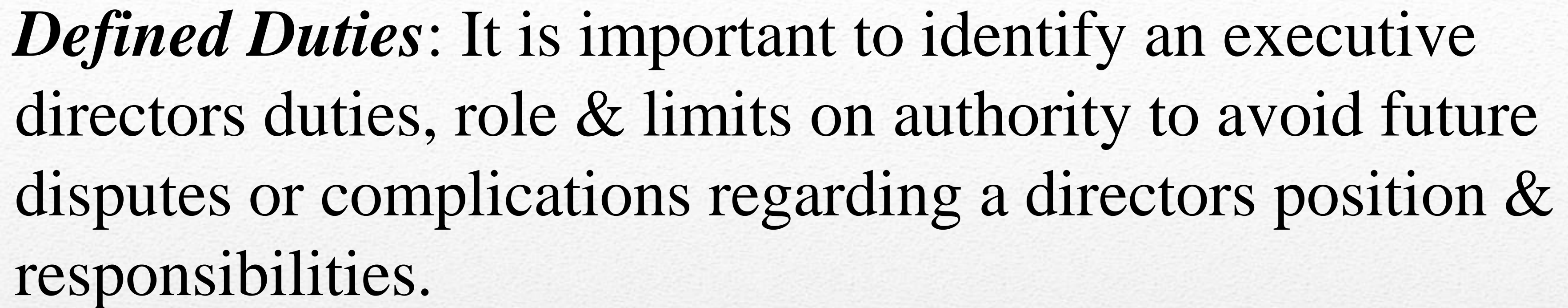
Service Contracts of Directors

A Directors service contract is a important document. Employment contracts for executive directors are commonly know as service contracts.

A directors service agreement commonly includes the following provisions;

Basic Provisions: These includes clauses concerning hours & place of work, salary, holiday entitlement etc.

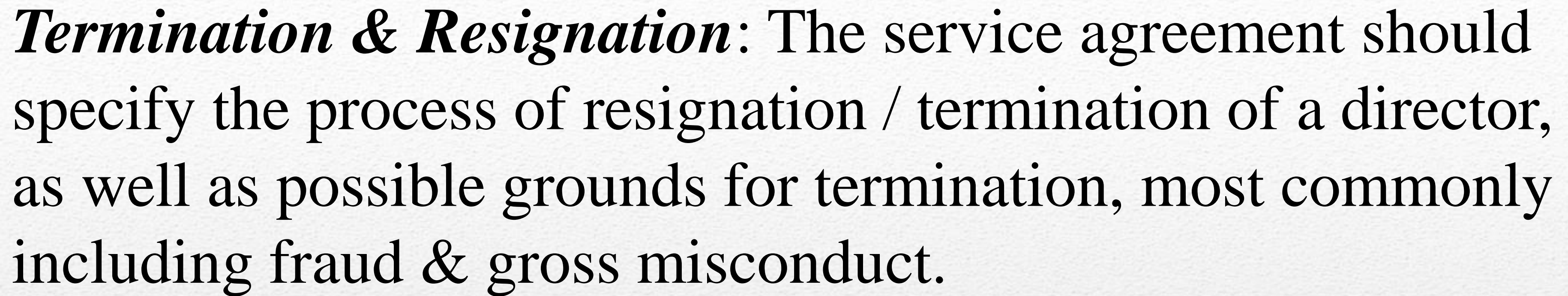
Bonus or Reward Schemes: provision could specify whether a director will be entitled to share options, bonus payments based on performance targets, medical insurance or expenses, life & disability insurance or pension options.



Defined Duties: It is important to identify an executive directors duties, role & limits on authority to avoid future disputes or complications regarding a directors position & responsibilities.

External Appointments: A service contract should clarify whether a director is permitted to work with other companies & if any restrictions apply to this entitlement.

Notice period :The notice period on which employment can be terminated is an essential provision of every employment contract. The appropriate length of notice will greatly depend on individual circumstances but is ordinarily between 6 & 12 months for senior directors.



Termination & Resignation: The service agreement should specify the process of resignation / termination of a director, as well as possible grounds for termination, most commonly including fraud & gross misconduct.

Restrictive Contracts & Confidentiality: Restrictive contract enable a company to protect itself against unfair competition & potential authorized use or disclosure of sensitive & confidential information, effectively safeguarding a company's relationship with its key customer & employees.

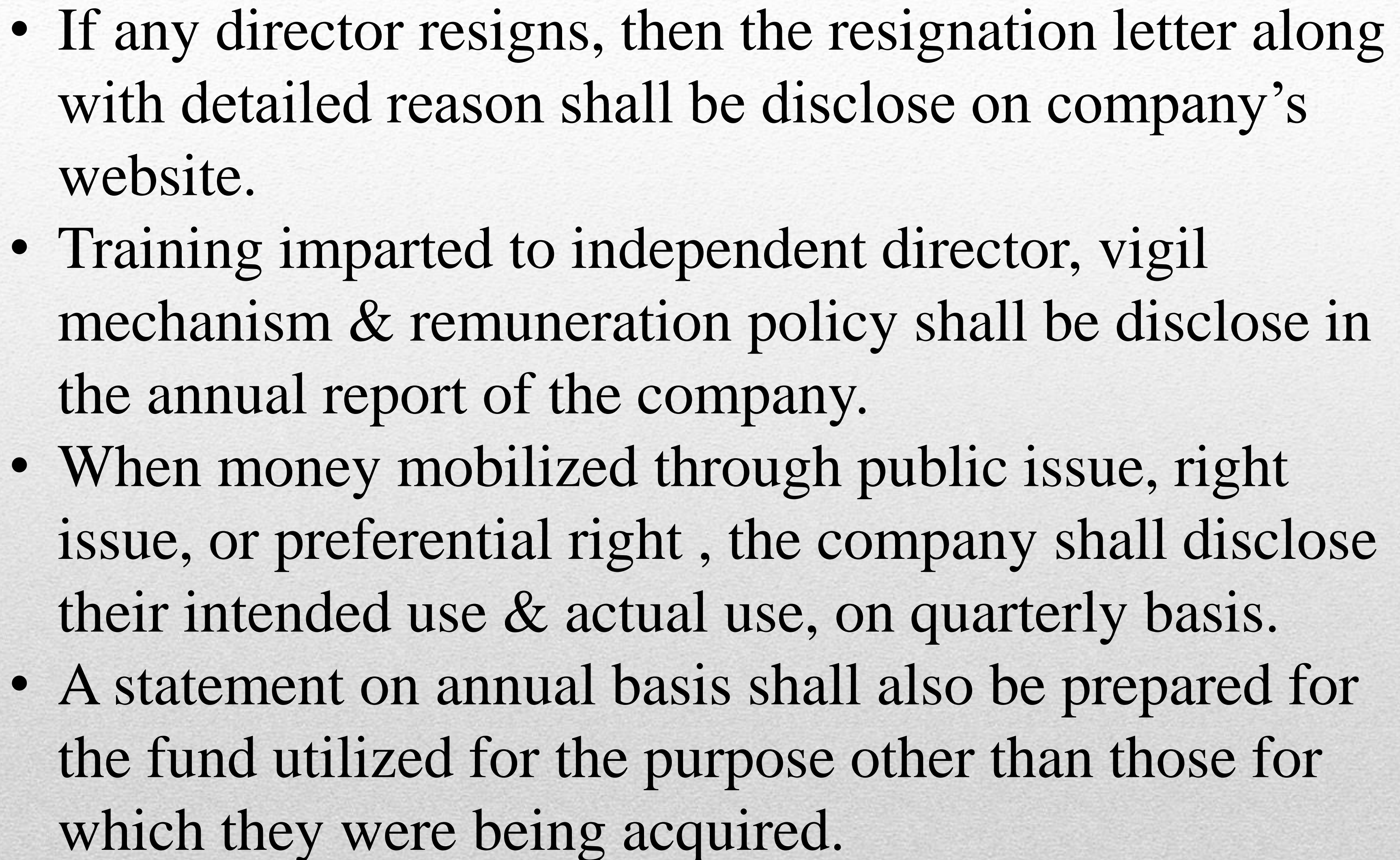
Directors service contracts with a guaranteed term is (or may be) longer than 2 years must be approved by an ordinary resolution of the shareholders of the company.

Financial Reporting of the Activities of the Company as per Clause 49

For good corporate governance company should make all necessary disclosures. It is the responsibility of management to make disclosures of all material facts which all stakeholders are suppose to know. Disclosures can be following matters;

- Related party transaction which is material in nature & policies for dealing with related party.
- Any accounting treatment, different from normal treatment & reason thereof.

- Remuneration to directors, facilities, perquisites etc. given to directors.
- Management disclosure & analysis report on various matters such as industry structure & development, opportunities & threats, segment wise or product wise performance, outlook, risk concern, discussion on financial performance.
- Transaction in which directors have personal interest shall also be disclosed.
- In case of appointment of new or reappointment of director some information about it like brief resume of director, nature of expertise in specific area, number of directorship in other companies.


• If any director resigns, then the resignation letter along with detailed reason shall be disclose on company's website.
• Training imparted to independent director, vigil mechanism & remuneration policy shall be disclose in the annual report of the company.
• When money mobilized through public issue, right issue, or preferential right , the company shall disclose their intended use & actual use, on quarterly basis.
• A statement on annual basis shall also be prepared for the fund utilized for the purpose other than those for which they were being acquired.

INTERNATIONAL FINANCIAL REPORTING STANDARDS(IFRS)

- IFRS are designed as a common global language for business affairs so that company accounts are understandable & comparable across international boundaries.
- IFRS set common rules that financial statement can be consistent, transparent & comparable around the world.
- IFRS are issued by the International Accounting Standards Board(IASB).

Standards IFRS Requirements

- Statement of Financial position: IFRS influences the ways in which the components of a balance sheet are reported.
- Statement of Comprehensive Income: This can take the form of one statement, or it can be separated into a profit & loss statement & a statement of other income, including property & equipment.
- Statement of Changes in Equity: Also known as a statement of retained earnings, this document the company’s change in earnings or profit for the given financial period.
- Statement of Cash Flow: This report summarizes the company's financial transactions in the given period, separating cash flow into operations, investing, & financing.

Objectives of IFRS

- ❖Help to standardize the diverse accounting policies & eliminate the incomparability of financial statements with an entity & across entities.
- ❖Facilitate the presentation of high quality, transparent & comparable information in financial statements.
- ❖Reduce to accounting alternatives & thereby eliminate the element of subjectivity in financial statements.

Need, Significance & Importance of IFRS

- Helpful to Accountants & Auditors
- Credibility & reliability to the financial statement
- Useful for comparison
- Global comparability
- Improve in accounting theory & practice
- Regulate corporate accounting
- Consistency
- Eliminate variation
- Contribute to economic efficiency
- High quality & transparency
- Reduce information gap

Disadvantages of IFRS

- Not Globally Accepted
- Manipulation of Standards
- Increased cost
- Not suitable for developing countries

Thank you …