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Manage

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SPECIAL ISSUE

MANAGEMENT CONCLAVE 2012

Effective Corporate Governance Through Vigilance

President's Message...

The BMA is well known for setting trends in Management. This is evident from the theme of the Management Conclave 2012, "Effective Corporate Governance Through Vigilance". The theme of this Conclave is not only timely but unique in itself as it is exploring avenues for ensuring effective corporate governance while reinforcing the existing corporate governance framework as aptly put in its objective.

The Conclave has been designed to benefit professionals, executives, academicians, scholars and various practitioners from the corporate world as well as from other sectors. Leading good governance and corporate governance practitioners have been invited as Speakers and Moderators to handle the Technical Sessions of the Conclave with the sub-themes, (i) Ethics & Management (ii) Transparency & Accountability and (iii) Compliance and role of Vigilance.

While the Conclave itself is going to enrich the delegates immensely, I am doubly glad that the Conclave Core Team is brining out a Special Souvenir during the Management Conclave 2012 containing articles and viewpoints from leading personalities particularly in the area of corporate governance.

I congratulate Dr. M.N. Krishnamurthy, IPS, Chairman of the Conclave and his eminent Team Members for their efforts for the success of this Conclave. My thanks are due to our Immediate Past President Shri N D Veeranna Gowda who continue to involve in this Conclave since from inception. The beautiful souvenir brought out on the occasion and the team effort to make it happen definitely deserves a special appreciation. I place on record our appreciation from the BMA on behalf of all the members towards this endeavor.

I am sure the Conclave would be a great success and would enormously benefit the delegates.

With best wishes,

Bangalore
August 2012

Dr. Manje Gowda
President, BMA

Chairman's Message...

The Special Souvenir is in your hands now as a 'take away' of some of the deliberations and viewpoints emanate from the Management Conclave 2012 on the unique theme 'Effective Corporate Governance Through Vigilance".

While the theme of the Conclave and sub-themes of the Technical Sessions were meticulously designed keeping in view the present trends and needs, the articles and view points contributed by the leading personalities have in fact turned out to be a real value addition to the Conclave and we are extremely glad to see this 'Special Souvenir' as the net result.

I, on behalf of the BMA and the Core Team, sincerely thank the leading personalities and other practitioners for having shared their thoughts and viewpoints on this important issue. I also take this opportunity to express our sincere gratitude for the Speakers and Moderators who readily agreed to participate in this Conclave and share their vast experience and expertise.

I would also like to place on record the support received from BMA Office Bearers and the officials of BMA in organizing this Conclave and brining out this 'Special Souvenir'.

On behalf of BMA, I wholeheartedly thank Shri G. Suresh, N.D. Veeranna Gowda, Dr. S.T. Ramachandra, N. Ravi Bhushan, S.S. Seetharamaiah, for their sincere and dedicated efforts in bringing out the Special Souvenir in a short time and making this year's Conclave a grand success.

I am sure, the ideas generated during the Conclave and shared through articles in the Souvenir would go a long way in achieving effective corporate governance in our country.

With best wishes,

Bangalore
August 2012

Dr. M. N. Krishnamurthy
Chairman
Management Conclave 2012
Sr. Vice President, BMA

Shri N.D. Veeranna Gowda, immediate past President, BMA deserves a special mention in this Edition. Because, he has been the pivotal force behind this Conclave, right from the conceptual stage and all through the execution, including this Special issue of "Manage".

Management Conclave 2012

Theme : EFFECTIVE CORPORATE GOVERNANCE THROUGH VIGILANCE

from 9.30 a.m. to 5.00 p.m. on 6th August, 2012
at Senate Hall, The Capitol Hotel,
Rajbhavan Road, Bangalore.

Inaugural Session :

Chief Guest : **Justice N. Santosh Hegde**
Former Lokayukta, Govt. of Karnataka

Presidential Address : **Sri. Pradeep Singh Kharola, IAS**
Principal Secretary to Chief Minister of Karnataka

Key Note Address : **Sri. H. S. Upendra Kamath**
CMD, Vijaya Bank

Technical Sessions :

Session 1 : Ethics and Management
Session 2 : Transperency and Accountability
Session 3 : Compliance and Role of Vigilance

"Leader's Speak"

"Corruption according to me makes a human, a sub-human, inhuman, not a human at all."

"Corrupt people have exhibited that they are not human beings. They will do anything to serve their greed."

"Meaning of the word 'democracy' which was said to be 'government of the people, by the people, for the people' has become 'government of some, by some, for some' and rest of India is just their servants."

"Unless the society is capable of distinguishing between legitimate wealth and illegitimate wealth and shun the people who have become illegitimately wealthy, we can never fight corruption."

"No democratic country can survive for long without a value based society."

VISION

To be the premier Institution in leading the Movement for Excellence in Management

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MISSION

Facilitate individuals and organizations to inclulcate best management practices, influence shaping superior public policies, pioneer new professional competencies and set ideal business environment.

Sri. V. Chokkalingam
Vice President, BMA

Sri. S. Prabhudev Aradhya
Hon. Secretary, BMA

Smt. Renu Lata Rajani
Treasurer, BMA

Conclave Core Team

Dr. M. N. Krishnamurthy, IPS
Chairman, Management Conclave 2012
Annual Conventions, Seminars, Workshops and Interface with Govt./Corporates

Dr. S. T. Ramachadra
Co-Chairman

Sri. G. Suresh
Convenor

Sri. N. Ravi Bhushan
Member

Sri. S. S. Seetharamaiah
Member

Conclave Theme : Effective Corporate Governance Through Vigilance

Objective

(i) To reinforce Corporate Governance framework and

(ii) To establish the role of Vigilance in enhancing Corporate Governance effectiveness

Preamble

Corporate Governance is a mechanism through which the values, principles, management policies and procedures of a corporate are delineated in consonance with its objective and matching with reality. Undoubtedly, ethical practices, transparency and accountability become the fundamental principles of good Corporate Governance. Thus the essence of Corporate Governance is to ensure transparency in all operation of the corporate so that accountability for the decision taken is fixed. Because, accountability is essential to ensure that the interest of the investors and the stakeholders covering customers, suppliers, employees and the society at large including environment, are safeguarded.

In a practical sense, therefore, Corporate Governance is all about the organisation embracing whole-heartedly a well-delineated structure to achieve its objectives and at the same time making a firm commitment to its shareholders and stakeholders all the time that their interests would be protected. The issue of Corporate Governance became highly and increasingly relevant not only in India but globally due to the financial meltdown starting with the Sub prime crisis in the United States and spreading all over the world. In fact, the root cause of the crisis were traced to lack of transparency, particularly on the basic issues like risk management and protection of interest of the investors and the stakeholders. When we look at from this perspective, the current financial crisis all over the world is perhaps a case of massive failure of Corporate Governance. Not only that. Failure of Corporate Governance affects practically all part of the society and the society could be a victim of malpractices in the corporate sector.

It is in this context, the Bangalore Management Association (BMA) found it appropriate to expand the horizon and explore the possibilities for effective Corporate Governance. From this point of view, there are two issues emerge, which assume importance when it comes to Corporate Governance in our country. Firstly, is it possible to rethink our entire approach to the issue of Corporate Governance in the country and device a better regulatory and monitoring system that will ensure that scams, particularly the Corporate scams are avoided in the future. Second is the role of watchdog agencies in ensuring Corporate Governance. When we think of watchdog agencies in Corporate Sector, we normally confine to the agencies under the Companies Act, the SEBI Act and so on. In fact, there is something called 'Vigilance', which is not so familiar in the Corporate Sector, especially the private sector.

'Vigilance' is something, which has not penetrated in to Corporate Sector, particularly the private sector. Of course, 'Vigilance' is not foreign to Public Sector organisations, which are also the leading corporate houses in the country. The public sector companies do have a full-fledged Vigilance department. In fact, senior officers of Union government from different organised services are designated as Chief Vigilance Officer (CVO) to head the Vigilance departments in the public sector companies on deputation to perform their job in a fair manner without jeopardising their position. The fact that the CVOs are given the status of Functional Directors of the organisation, speaks volume for itself on the role and contribution expected of from them. Then the obvious question comes. How could Vigilance contribute in a Corporate Sector for that matter Corporate Governance? Well, the answer is quite obvious too!

Anyone who is alien to Vigilance and the role of CVO in a public sector organisation, if start knowing about it, would immediately hop up to say, 'oh, they are very much into the Corporate Governance issues'. This is the key issue of the Conclave. BMA is, indeed, very glad to chose the theme for the Management Enclave 2012 as 'Effective Corporate Governance through Vigilance" with the sole aim to drive home the point that there is yet another avenue available in 'Vigilance', which is very much in practice, to enhance the effectiveness of Corporate Governance.

Against this backdrop, BMA has designed three Sessions for this Conclave, namely, Ethics & Management, Transparency & Accountability and Compliance & Role of Vigilance, for deliberation involving Academicians, Policy Makers and Practitioners. BMA is very confident that this expansion of horizon of Corporate Governance engulfing vigilance would go a long way in enhancing its effectiveness.

Inside...

EFFECTIVE CORPORATE GOVERNANCE THROUGH VIGILANCE

N. Vittal, IAS (Retd.)

The theme for this year's Management Conclave could not have been more appropriate. In the last three years we have witnessed dramatic developments, which closely and directly linked to the governance and the economy of the country and the perception of the rest of the world about our country itself. Three years ago, we have been hailed as an emerging power, both politically and economically. Our growth rate was the envy of the developed world. India was clubbed with three other economies and was one of the prominent pillars of global economic growth known as BRIC (Brazil, Russia, India and China).

Unfortunately, today, India seems to be the first BRIC falling down. The rating agencies are downgrading our country and the rupee is also falling in value. India is perceived to be a corrupt country, where crony capitalism flourishes and therefore no longer is able attract the level of investments which we were expecting. The Time magazine's recent comment about our Prime Minister as an under achiever is the latest in the barrage of negative comments made about our country in the media and many other forums.

By a curious coincidence, there seems to be unanimity of views so far as the Indian corporate sector and the foreign commentators about what is wrong with our country today. It is policy paralysis. India today, is in a position to make an effort to keep up the momentum to realise economic growth and all round development and fulfil its promise of being a very important and globally dominant economic power, but there seems to a great reluctance in the Government circles to take the right policy decisions. This policy paralysis from the corporate sector's point of view is directly attributed to the series of scams that have exploded in the public domain in the last three years and the perceived over activity of the regulatory agencies, especially the Vigilance bodies like the Comptroller and Auditor General of India, the Central Vigilance Commission and of course, the Supreme Court. In short, today, vigilance activity and investigative media ever ready for breaking news to capture the eye bolls of the viewers seem to have lead to the continuous 24 x 7 quest for the scandals, however, small or big. Once the scandal is detected, it is flogged to death, till the next scandal is identified. The net result is, even genuine committed honest executives are paralysed into inaction. In a country where the government had played a prominent role since independence in the economy, this has led to a policy paralysis. Surprisingly, even the liberal economies of the west where the government's role in the economy was relatively less, are finding that increasingly, the government has to play a role in the economy, thanks to the consequences of the global financial meltdown of 2008.. This meltdown was directly attributed to the unbridled actions of the experts in the financial services sector, driven by a sense of insatiable greed forever looking for new financial instruments and creative financial engineering for maximising their quarterly profits. While this global economic meltdown did not affect India directly to the extent feared, thanks by and large, the Reserve Bank of India, which had followed a conservative policy, the fact still remains that the delayed impact of the global financial meltdown is having its toll on the Indian economy. That act of the RBI provides the linchpin for the theme connecting corporate governance and vigilance.

To go back a little in history, it was in the late 1990s or 1997 to be more precise that the time of the South East Asian economic crisis took the hitherto much acclaimed South East Asian Tigers became paper tigers, thanks to borrowing short, lending long , forgetting the basic fundamentals of good financial managements, 'Corporate governance' became a popular expression of the lexicon of global economic discussion. Suddenly, the world was rediscovering the fact that honesty was after all the best policy. As the Economist summed up, the three lessons that were re-learnt were : 1. Be frugal, 2. Be prepared and 3. Be honest.

A clear distinction was made between good corporate management which involves using the best management skills taught in the business schools in an enterprise to achieve goals like profitability, quality, productivity and market capitalisation. Corporate governance meant the moral framework, the ethical framework and the value framework under which business decisions were taken by the management of an enterprise. It was found that the very fact that a company had the best corporate management in terms of traditional skills in management like profit maximisation, productivity improvement, market capitalisation was no guarantee for the long time viability of an enterprise. Many of the Fortune 500 companies met their waterloo and this was again repeated in the year 2000 at the time of Dotcom bust. Much admired companies like Enron, Worldcom and so on were found to be financially unviable and became bankrupt. Not only this, but even well established companies which had long record of reputation like companies like the accounting and auditing firm Anderson were exposed to be having clay feet, because they suffered from a conflict of interest between the clients whom they audited and whom they also advised as consultants so far as risk management is concerned. The world rediscovered the importance of the ethics in business and corporate governance became the buzzword for healthy and ethical running of enterprises.

In the ultimate analysis, what is the essence of corporate governance? A clear understanding of the basic facts is vital to appreciate the link forming a virtuous cycle between vigilance and effective corporate governance.

The essence of corporate governance is three.

(i) Transparency. This is vital, because, without transparency, the process by which key strategic decisions are taken in an enterprise remain opaque. If we want effective vigilance corrupt and dishonest practices must be totally avoided.

Sunshine is the best antidote to corruption. Transparency means sunshine. Vigilance is vital for effective corporate governance QED.

(ii) If the decision-making is not transparent, then we miss the second important aspect of corporate governance, which is accountability. After all those who take decisions must be held accountable.

(iii) This brings us to the third important aspect - accountability for what?

This will depend upon a wide range of issues. At a very narrow level, it may mean accountability to those who are investors and a little broader view would cover all the immediate stake holders in the enterprise like the customers, the employees, the suppliers who are immediately concerned with the running of the enterprise. And at still further level, stakeholders would include not only the immediate stakeholders like the customers, suppliers and investors, but society at large. And at a still further different dimension, the society would also include the physical environment, especially concerns about global warming and pollution, which could be the direct consequences of running of the enterprise.

In short, transparency, accountability and safeguarding the interest of the stakeholders are the three pillars of corporate governance. Having recognised the central importance of corporate governance, we come to the basic question and the earlier reference to policy paralysis in our country where overall vigilance bodies are given as the main reason why decision-making has come to a grinding halt.

In fact, vigilance in a sense means alertness. In the context of a corporate enterprise alertness would mean ensuring that the decisions taken in an enterprise are not illegal or do not involve malpractices. Corruption is lack of integrity in a broad sense. This would include intellectual, moral and financial integrity. Corporate governance focuses on the moral dimension and it is necessary to have clarity of thoughts so far as what is moral or ethical.

The three-point test Norman Vincent Peale and Kenneth Blanchard in their book, 'The power of ethical management' is a useful guide. To be sure whether any decision you take is ethical or not, apply this three point test. 1. Is it legal? If the decision is not legal, it is basically unethical. 2. The second is, is it fair? If it is not fair to all parties concerned, then such a decision is also unethical. As we have seen corporate governance involves accountability to the immediate stakeholders and the society at large as well as the environment. In the context of corporate governance in a wider sense, the decision taken must be fair to all the parties concerned. 3. The third test is a test, which the ultimate test. If the decision taken becomes public knowledge, will it cause embarrassment to you or your enterprise and colleagues?

The series of scams we have witnessed from 2010 onwards, 2G, CWG and the Adarsh scam so on, have been cases where decisions were taken in a colourable manner and when they became public, they caused embarrassment and much more to all concerned with the decision making. Because of this, the entire atmosphere in the country has changed today. 2010 was the year of scams, when one scam after another starting with 2G scam, CWG scam and the Adarsh scam and scams relating to even the Chief Justice of the Supreme Court were exposed. Year 2011 was the year of reaction by the civil society led by two powerful charismatic leaders Anna Hazare and Baba Ramdev. The third year 2012, is perceived to be the year of judgement, where we see the impact of the issue of corruption on politics.

Politics anyway has not become free of corruption. In fact, Indian politics today seems to be a game of muscle power and money power. Nevertheless, there are silver linings, like: (1) The implementation of Right to Information Act and its increasing use by the activists, (2) Activism of the Supreme Court which has come out with concepts like the 'institutional integrity' as articulated in the case of Justice Kapadia's judgement in the PJ Thomas case as CVC and (3) the increasing concern of the political parties at least for sheer survival to appear to act as if they are facing corruption.

In this context, therefore, we come to face the basic issue. It appears that in a democracy like ours, what is politically good is economically bad. Good economics seems to be bad politics and vice versa. In a different level therefore, if integrity is required for ensuring good corporate governance, is it against business success? Can honesty in business and good corporate governance go along with a highly competitive globalised economy where 'get on, get honour and get honest' seems to be the route?

From my experience with government and also interaction with the industries, I would like to make a simple suggestion to resolve the issue and also ensure that while one maintain highest standards of integrity in decision making in enterprise, one can also be successfully running a corporate enterprise by observing the principles of good governance. Or in other words, effective corporate governance can be achieved through vigilance. This vigilance depends upon building in the values of integrity in the system itself. It may be recalled that years ago, Peters and Waterman came with a classic book in 1982 of 'In search of excellence'. They said that one of the characteristics of excellent companies was 'hands on value driven'. The trick is how to ensure that we build an ethical enterprise by designing systems and procedures so that the ethical values are reflected and practiced by everyone in the organisation from the highest level to the lowest. Fortunately, we have got very good models available through out and one need not reinvent the wheel. For example, in the private sector, there have been companies like TATAs, Infosys, Mahindra, TVS Group, who have been practicing the highest ethical standards without at the same time losing their position in the market. The practices adopted by these companies in the indian context provide a guideline by which there can be effective vigilance and at the same through effective vigilance good corporate governance can also be achieved.

Apart from designing systems and procedures on the model of exemplary companies, I would also like to emphasis one basic point for long term success. Ultimately, it is the question of finding the right person for the right job. This can be achieved only by what I would call a 2T process. Transparency in the qualities needed for selecting a person to a job and the selection process itself should be transparent so that nobody questions the selection. Secondly, there should be another 'T'. This is the TINA factor (**T**here **I**s **N**o **A**lternate). In the selection process itself, a system must be so designed that there is no alternative but to select the right person. Once we bring in the 2T elements in our system of handling human resources in any enterprise, automatically, it will ensure that there is good vigilance and effective corporate governance.

Finally, as an individual, my advice to the executives in any enterprise, whether in public sector or private sector will be as follows:

1. If you want to be successful and at the same time ensure good corporate governance in your enterprise, you yourself must be honest of having intellectual, moral and financial integrity.

2. Before you take any decision, apply the three-point test of Norman Vincent Peale and Kenneth Blanchard mentioned above.

3. Always record reasons in real time, when you take any decision. Many a time, we may say there is no time to record decision, but I have found that if in the heat of the moment and in the pressure of circumstances when we take decisions and certain nuances are appreciated and that is why we take those decisions. But if we delay recording decisions, then some of the relevant points will be missed and one can come to trouble later on when the 20:20 vision of audit and hindsight are applied. I have always used a Dictaphone in the last two decades of my career and recorded reasons for decisions in real time. I used to even record the minutes of the meeting which I headed especially when it involved other ministries in government of India, so that no point is lost and the very fact that we have to record in presence of the other members of the meeting in real time imposes an automated discipline that ensures transparency and honesty.

The author is former Central Vigilance Commissioner and recently awarded Padma Bhushan

Comparison of guidelines of Clause 49 of Companies Act, India and Sarbanes Oxley Act, US

Topic	Clause 49 (Listed companies)	US-SOX & Other Laws
Board	- Independence - Internal Control System - Disclosure & Code of Conduct	- Independence (gen.majority) - Internal Control system - Disclosure & Code of Conduct
Audit Committee	- Independence (2/3) & Financially Literate - Review audit & internal audit	- Independence & Financially Literate - Review audit & Internal audit
Disclosures	- Compensation - RPTs - Risk Management & Accounting Standards - Use of Proceeds	- Compensation - RPT's - Risk Management, etc...not required, but generally provided. - Use of Proceeds
Certifications	- CEO & CFO - Financials, Internal Control, Comply with Laws, Changes in Policy	- CEO & CFO - Financials, internal controls, etc...
Compliance	- Certificate on this. - Disclosure compliance or not with mandatory and non-mandatory req'ts.	- Similar, but no requirement to disclose if meet non-mandatory req'ts.
CG Reports	Quarterly	- Not required though often provided
Subsidiary	- Significant issues report to parent board. - Independent directors.	- Generally required to report important issues as per state corporate law.
Non Mandatory	- Training - Whistleblower policy - Evaluate non-executive board - Limits on independence	- Whistleblowers much more prevalent - Training not required, but often provide. - Performance evaluation - Greater discussion on compen. levels
Penalties & Enforcements	De-Listing	- Large criminal penalties (individuals & companies) - Large civil penalties (public & private).

(Source http://www.nfcgindia.org/pdf/corporate_governance_report.pdf)

INTERVIEW WITH SHRI H S UPENDRA KAMATH, CHAIRMAN & MANAGING DIRECTOR, VIJAYA BANK FOR SPECIAL SOUVENIR TO BE PUBLISHED ON THE OCCASION OF MANAGEMENT CONCLAVE ON "EFFECTIVE CORPORATE GOVERNANCE THROUGH VIGILANCE CONDUCTED BY BANGALORE MANAGEMENT ASSOCIATION

Q 1 The theme of this year's Management Conclave is 'Effective Corporate Governance through Vigilance'. How appropriate, you think, is the theme at this point in time ?

Ans: In my personal view, the above theme is most appropriate at this point in time. Corporate Governance is nothing but evolving and adopting certain set of values and ethics for the functioning of corporate entity with a view to maximizing the value for all its stakeholders. This includes not only the shareholders but all others connected with it directly or indirectly. It also includes the society and nation at large. Corporate Governance is more relevant at this point of time against the backdrop of what is happening in the business world of late with many scams and unethical practices coming to light and the magnitude of its impact on all the concerned. Hence, there is no doubt that the theme of the Management Conclave is highly relevant in the present day context.

Q 2 Corporate Governance is a buzz word now. What do you think is the reason for this ?

Ans: Corporate Governance has acquired more importance of late. One strong reason for this, which is coming to my mind is evolving corporate culture. In other words, the corporate world is rapidly moving from the family dominated personalized culture to highly professionalized approach. In this environment Corporate Governance assumes great significance unlike in the other mode where the individualistic preferences drive the decision making. Yet another reason for the growing importance of Corporate Governance has been globalization, which has with it brought in new benchmarks and standards for corporate functioning. Increasing public awareness & judicial activism too is an important factor for growing significance of Corporate Governance as nobody can take things for granted now. Right to Information is the latest development which necessitates that all the affairs of an organization should be carried out in an orderly and transparent manner. I think these are some of the important factors which made Corporate Governance a buzz word now.

Q 3 How could one differentiate Corporate Governance from Corporate Management ?

Ans: Corporate management is concerned with the general process of decisions making within a company. On the other hand Corporate governance as explained earlier is the set of values, principles and practices aimed at serving the interest of all of its stakeholders. To cite an example, taking a decision for purchasing an asset of huge value is concerned with corporate management but carrying out the same in a highly transparent manner complying with the established systems and practices in the best interest of all concerned is Corporate Governance.

Q 4 Is Corporate Governance in the banking sector different from other sectors ?

Ans: No. But, I can say that it is more pronounced and significant in Banking in the sense that as bankers we are dealing with public savings and hence, has an additional dimension to it.

Q 5 What are the major corporate governance issues which you faced in your banking career ? Have you ever had any dilemma while handling such corporate governance issues ?

Ans: In Banks, we have well defined process which governs various spheres of our activities. These policies are well deliberated and approved at Board level. Exceptions/ Deviations are provided for along with set procedure for seeking ratifications. Breaches are kept to the minimum most and are always driven by business needs/interest. There are various committees of the Board which look at various activities of Banks. Thus, Corporate Governance ethos are well entrenched in Bank's working. Personally I have had no dilemma thus far on Corporate Governance matters.

Q 6 Corporate Governance is the flavor of the day, particularly after the exposure of corporate scams. What according to you are the main reasons that lead to the corporate scams, particularly in India ?

Ans: Absence of well defined laid down systems and procedures, relegating moral and ethical values to sidelines in order to achieve the desired results in whatever ways and means, public indifference and general apathy to what is happening around, pandering to the well entrenched

vested interests in power by the corporates in order to get their work done, laxity on the part of various authorities concerned with are some of the reasons why scams are happening in corporate world, especially in India. Added to this, there is always a human factor to it in the form of greed.

Q 7 You have been with the Indian Banking Sector for many years now. How do you see the corporate governance issues help the banking industry ?

Ans: As I explained earlier, Corporate Governance is more significant in Banking because we are dealing with the hard earned savings of public at large. So, it is our primary duty to take care of public savings. We have been entrusted with a pious duty of augmenting the public savings by offering them remunerative return and investing them in a very judicious manner to earn fair amount of return to pay our shareholders. Further, as a public sector bank we have a responsibility of social obligations while lending and offering banking services. Hence, in order to enable us to fulfill all these obligations, it is necessary to conduct all our affairs in a fairly transparent and professional manner as they are under the close scrutiny of public. Therefore, a good Corporate Governance would help us to perform our job in a highly professional and transparent manner, which would in turn enhance our credibility in the market and raises confidence of all our stakeholders.

Q 8 What according to you are the ultimate measures of good corporate governance ?

Ans: While there is no doubt that the essence of good corporate governance is ensuring trustworthy relations between the corporation and its stakeholders, taking care of their interest and enhancing their value, it also involves a lot more than compliance. Good corporate governance is a culture and a climate of Consistency, Responsibility, Accountability, Fairness, Transparency, and Effectiveness.

Q 9 Is it fair to say that vigilance actually helps in ensuring internal controls which in turn lead to good corporate governance ?

Ans: There is no doubt in it. Existence of sound vigilance practices enhance the strength of internal controls, which in turn ensures carrying out operations in an organization in a fair and transparent manner, which is the essence of Corporate Governance. Preventive Vigilance also has a pivotal role to play. It is not enough to punish the guilty. It is equally important to create a culture and awareness for all to avoid pitfalls.

Q 10 If 'Vigilance' really do contribute towards effective Corporate Governance, what do you think the measures to be adopted by the Vigilance Professionals ?

Ans: In order to effectively contribute to Corporate Governance, Vigilance need to be positive in its approach. Vigilance stance should be supportive of achieving overall business objective of the organization and should not come as a hindrance on its way. Positive Vigilance should pre-empt the occurrence of undesired events, train the people to face such events and handle it rather than going after the innocents who are involved in such eventualities by accident. In short, it should act as "Watch dog" and not as a "blood hound".

Q 11 Any other views you would like to share with us on the issue of Corporate Governance and Vigilance.

Ans: In my view Vigilance should act as a contributing, supplementing and supporting factor to Corporate Governance and should not override it. Vigilance should engage in devising sound policies and practices to enable the organization to conduct its affairs in the best possible manner without placing obstacles. Such vigilance would certainly help a robust corporate governance contributing to the overall well being of the organization.

"We are responsible for actions performed in response to circumstances for which we are not responsible."

Allan Massie (1938-), British author
Source : "Etienne," *A Question of Loyalties* (1989), pt. 3, ch. 22

"A business that makes nothing but money is a poor kind of business."

Henry Ford (1863–1947), US industrialist, automobile manufacturer and founder of Ford Motor Company
Source : Quoted in *The Arizona Republic* (1999)

VIGILANCE – THE RIGHT OPERATING SYSTEM FOR GOOD CORPORATE GOVERNANCE

G. Suresh

'Operating System', in computer parlance, is known as the system software, which is responsible for the running of the computer and management of computer resources. DOS, UNIX and WINDOWS series are the best-known operating systems, which the computer world has seen so far. Every software or application software requires any one of these operating systems to operate. Similarly, when it comes to corporate governance, it is better governed when it operates on an operating system, which has the best compatibility and also produces effective results. This brief study demonstrates how vigilance acts as the operating system for good corporate governance.

The approach in this paper is through three parts namely, (i) Corporate governance (ii) Vigilance and (iii) Interface between corporate governance and vigilance.

(i) Corporate Governance

Corporation - as welfare state[1]

Article 38 of the Constitution of India envisages the concept of "State to secure a social order for the promotion of welfare of the people". It was through the industrial policy resolution of 1956 that the Government perceived Public Sector Undertakings as a potential instrument of socio-economic development with a view to develop the 3 major areas namely (i) a sound agricultural and industry base (ii) to overcome economic and social backwardness and (iii) generating sufficient surpluses. It was the compulsion of time that the Government of India invested huge amount in the public sector undertakings for the socio-economic development. An amount of Rs.29 crores was invested in 5 Public Sector Enterprises (PSEs) in 1951 for the economic development. The number of PSEs rose to 214 in 1984 with an investment of Rs.35,411 crores.

According to the Special Chapter on 'Vigilance Management in Public Sector Enterprises' published by the Central Vigilance Commission[2], PSEs account for a public investment of Rs.2,04,054/- crores, spread over 240 Enterprises. The original purposes, for which these Enterprises were set up, varied and included such objectives as:

(a) setting up of an infrastructure for rapid industrial growth;
(b) creation of additional employment opportunities;
(c) facilitation of balanced regional development;
(d) generation of surplus funds for further investment for economic development; and
(e) reduction in disparities in income and wealth through prevention of concentration of economic power in private lands.

Even though profit making was considered as the major objective of the PSEs, they were entrusted with more social responsibilities rather than profit making as the prime objective, particularly in the absence of private players with exceptions to Tatas and Birlas. Therefore, Public Sector Enterprises, in the hands of the Government were considered as the only means for economic development of the nation in the post-independence era in India.

Shift of onus

It was till the time of economic reforms in the early 90s followed by the liberalization processes, the onus of economic development of the country lay with the Government. However, with these reforms and liberalizations having got shapes, they facilitated the entry of global companies, multi-national investors and other private sector companies. With these developments, the main function of economic development of the nation, till then with the government, got a tilt and the onus got a shift towards the non-governmental sectors. Thus, not only in India, but also all over the world a significant transformation in the role of non-governmental sectors i.e private sectors in the economic development were witnessed. The basic objectives, for which the public sector undertakings were set up namely industrial growth and employment opportunities etc., were taken over slowly by the private sector. Therefore, the compulsion of the government to have public sectors for the economic development has become an option in the hands of the government in view of the role being played by the private sector in the economic development, in the post-liberalization era.

This onus shift of economic development in the post economic liberalization scenario and subsequent competition generated within the private sectors and also between the private and the public sector have forced the corporate world to became self-reliant and profit making centers and at the same time face the challenges posed by competition. It is in this context the corporate governance assumed significant importance not only for the public sector, but also for the private sector and in the sense, for the entire corporate world.

Corporate Governance

Corporate governance, just a decade ago was hardly a subject discussed in any forum in India. It was almost non-existence in public domain. It has become a relevant issue today because of the emerging economy due to the integration of Indian economy with the global economy.

The importance of corporate governance in the Indian context can be seen from the foreword to the code of CII[3], which led to the setting up of the Rahul Bajaj Task Force on Corporate governance. This says, "In recognition of the key importance of corporate governance at this time when the Indian economy is integrating with the global economy and Indian industry is striving for international competitiveness, the CII National Council considered it essential to take a special initiative and set-up a National Task Force on Corporate Governance"

What is Corporate Governance?

According to Richard Smerdon[4], the expression "corporate governance" was not uncommonly found in American law journals in the 1970s. Later on, it was imported from America into the UK in May 1991 when the financial scandal broke out and thus the infamous Cadbury Committee on the financial aspects of Corporate Governance was born out of the scandals. The Cadbury Committee Report was published on 1st December 1992, which defined corporate governance as "the system by which companies are directed and controlled". There are several definitions prescribed over the period of time. Some of the commonly known definitions available in the public domain[5] are:

- "Corporate governance is a field in economics that investigates how to secure/motivate efficient management of corporations by the use of incentive mechanisms, such as contracts, organizational designs and legislation. This is often limited to the question of improving financial performance, for example, how the corporate owners can secure/motivate that the corporate managers will deliver a competitive rate of return", *www.encycogov.com* **Mathiesen** (2002).
- "Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment", *The Journal of Finance*, **Shleifer and Vishny** (1997 page 737).
- "Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, mangers, shareholders and other stakeholders and spells out the rules and procedures for making decisions on 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", **OECD** April 1999, OECD's definition is consistent with the one presented by Cadbury (1992, page 15).
- "Corporate governance- which can be defined narrowly as the relationship of a company to its shareholders or, more broadly, as its relationship to society, from an article in **Financial Times** (1997).
- "Corporate governance is about promoting corporate fairness, transparency and accountability" Wolfensohn, president of the **World Bank**, as quoted by an article in Financial Times, June 21, 1999.
- "Some commentators take too narrow a view and say it (corporate governance) is the fancy term for the way in which directors and auditors handle their responsibilities towards shareholders. Others use the expression as if it were synonymous with shareholder democracy. Corporate governance is a topic recently conceived, as yet ill-defined, and consequently blurred at the edges… corporate governance as a subject, as an objective, or as a regime to be followed for the good of shareholders, employees, customers, bankers and indeed for the reputation and standing of our nation and its economy" **Maw et al** (1994, page 1).

Transparency and accountability

Therefore, in a crispy term, corporate governance can be defined as "Enhancing the return on capital through increased accountability". It is, in fact, the mechanism by which values; principals, management policies and procedures of a company are made in consonance with the real world. It refers to the entire system by which the company is managed and monitored in a transparent manner. ***Undoubtedly, transparency and accountability are considered as the two fundamental principles for good corporate governance.*** In a practical sense, corporate governance provides a structure through which the objectives of the organizations are achieved and the performance monitored from time to time.

Corporate governance has several claimants – shareholders and other stakeholders include suppliers, customers, creditors, the bankers, and the employees of the company, the government and the society at large. The right starting point for good corporate governance is the high degree of priority on the interests of the shareholders who have immense faith in the Corporations to use the investment funds wisely and effectively.

Corporations or Corporate are the republics. In any corporate sector, the ultimate authority rests with the shareholders or the shareowners. The shareholders are the owners. They elect the representatives called the Board of Directors. The Board of Directors delegates most of the decisions to Managers down the line, for effective management of the affairs of the Corporation. In any case, the ultimate objective of any Corporation is to protect the interests and rights of the shareholders or shareowners. As in the case of any republic, the actual power sharing relationship depends upon the specific rules of Governance.

Good corporate governance involves a cohesive set of relationships among the Board of Directors, management, shareholders and stakeholders of an organization. Researchers have found that "Firms with stronger shareholder rights had higher firm value, higher profit, higher sales growth, lower capital expenditure and fewer corporate acquisitions". The Board of Directors represents the interests of the company's shareholders i.e. the owners of the Corporation in optimizing long-term value by providing the company with proper guidance and strategic vision on behalf of the shareholders. In the recent times the usage of word 'shareowner' is being used instead of `shareholders' particularly in the case of public sector enterprises, perhaps, it is because the Government holds the major shares in it. Equally important is the responsibility of the Board to ensure that the company's management and employees operate with the highest degree of ethical standards.

Corporate governance, therefore, is only part of the larger and economic context in which the funds of the shareholders operate. However, sustenance and long term success of a company depends on the factors such as business ethics and corporate awareness of the environmental and societal interest of the communities in which it operates. The degree to which Corporations observes the basic principles of good corporate governance is considered increasingly as an important factor.

Matter Ethics

According to Shri Narayana N R Murthy,[6] "Rules cannot substitute for character. It is ethical behaviour that will ensure that the CEO and the internal members of the board or the senior management behave properly. Decent and desirable behaviour goes beyond the domain of rules that are mandated. Remember that the rule of law cannot defeat the perversity of the heart".

Lord T.B. Macaulay considered the ultimate test of ethics as, "*The measure of a man's real character is what he would do if he knew he would never be found out".*

The importance of ethical standards for good corporate governance was emphasized by the OECD.[7] In its declaration on corporate governance, the OECD relates it to the internal means by which corporations are operated and controlled. This views of OECD is in consonance with the Cadbury Committee, which defined the control environment factors to include "integrity, ethical values and competence of the entity's people, management philosophy in operating style, the way management assigns authority and responsibility and organizes and develops its people and the attention and direction provided by the board of directors".

Internal Controls

In their book "Winning ways through Corporate Governance", Neville Bain & David Band,[8] illustrates the hierarchical approach of corporate controls, based on the observation of the COSO report. The control level includes the following:

Level	Includes
Corporate controls	- Corporate policies - control culture and values - audit committee
Management controls	- planning and performance monitoring - accountabilities - risk evaluation
Business process controls	- authorization - validation - reconciliation
Transaction controls	- accuracy checks in detail - consistency - completeness - compliance

In the Indian context also, the importance of internal control has been emphasized to a greater extent in the corporate sector. For instance, Shri Narayana N R Murthy has emphasized the importance of internal control as: "It is important for companies to have effective internal controls in order to ensure good corporate governance standards. The annual report should contain a report of the audit committee on their satisfaction of the measures taken during the period to strengthen such internal controls. Right now, in India, this is mandated only for listed companies. However, we should extend this to include the subsidiaries of public companies as well". While governments play a central role in shaping the legal, institutional and regulatory climate within which individual corporate governance systems are developed, the main responsibility lies with each corporation.

Shri KRS Murthy,[9] views that sociological and evolutionary approach is required to improve governance practices. According to him, "the problem in corporate governance is the achievement of a balance between autonomy for management and accountability to the organisation's various stakeholders". He further says, "the asymmetry in autonomy and accountability and the need to provide room for desirable new initiatives under changing technological conditions, levels of risk and uncertainties is at the heart of the corporate governance problem".

However, in the words of Hampel Committee.[10] "Corporate governance is not just a matter of prescribing particular corporate structures and complying with a number of hard and fast rules. There is a need for broad principles".

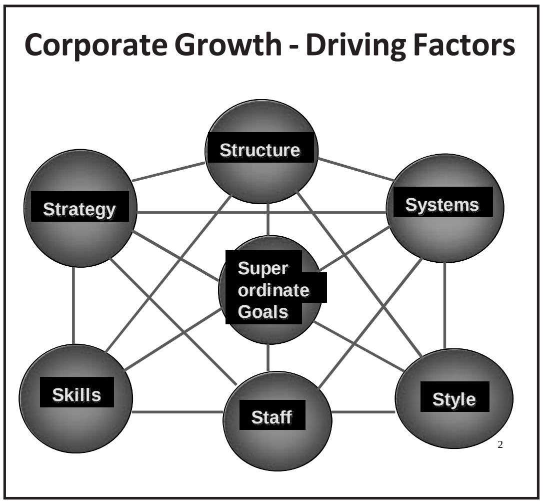
The Committee on corporate governance appointed by the SEBI[11] on May 7, 1999 *agreed that the fundamental objective of corporate governance is the* **"***enhancement of shareholder value***,** *keeping in view the interests of other stakeholder".* This definition harmonizes the need for a company to strike a balance at all times between the need to enhance shareholders' wealth whilst not in any way being detrimental to the interests of the other stakeholders in the company.

The Committee further observes, "Structures and rules are important because they provide a framework, which will encourage and enforce good governance; but alone, these cannot raise the standards of corporate governance. What counts is the way in which these are put to use. *The Committee is thus of the firm view, that the best results would be achieved when the companies begin to treat the code not as a mere structure, but as a way of life."*

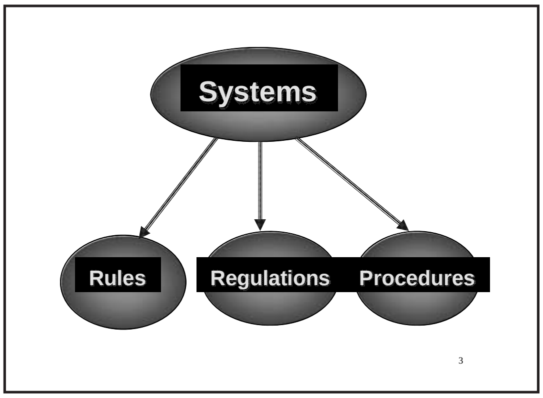
Therefore, transparency, accountability and ethical standards are considered as the three engines, which drive corporate governance. Convergence of these three aspects in order to have good corporate governance is possible only through internal controls. The internal controls can be achieved only with proper system in place.

Exercise of internal control

According to McKensay, there are seven driving factors in the corporate management framework. Popularly known as 7S framework, it prescribes that each one of the factors dependent on each other to a greater extent. They are interlinked as follows:



It is the system, which contributes for good corporate governance by way of internal controls. Either it is a private sector or the public sector, in order to have internal controls, it is imperative that the systems are in place. After all the systems are nothing but the combination of Rules, Regulations and Procedures, which best suitable for each corporation.



Therefore, existence of systems is considered as the most important factor for good corporate governance. Equally important is the fact that such systems in place are followed. Otherwise, having a system and not following the same would tantamount to non-existence of the system itself. Therefore, it is in this context, Vigilance comes in to the picture.

(ii) Vigilance – to operate the internal control

Before introducing 'vigilance' to the arena of corporate governance, it is better to know the track record of vigilance in order to appreciate the concept in its proper perspective. Therefore, a brief description on vigilance is given here:

Traces of vigilance

The word 'Vigilance' is even traced during the time of Shakespeare[12]. For example in 'Tempest', 'Antonio' speaks to Sebestian:

> ***"Let it be tonight;***
> ***For, now they are oppress'd with travel,***
> ***They***
> ***Will not, nor cannot, use such vigilance.***
> ***As when they are fresh"***

The earliest reference of a formal vigilance committee is available in the American history as early as the American Revolution. It was a self-appointed committee primarily meant for maintaining law and order and justice before effective governmental organization emerged. These committees summarily dispensed justice through various methods like banishment, whipping or hanging the persons they consider guilty. After the adequate law enforcement machinery was established, these committees and other vigilance groups gradually disbanded voluntarily.

What is vigilance?

Vigilance has been defined in the Oxford English Dictionary as the 'quality or character of being vigilant, watchfulness against danger or any action on the part of others, alertness or closeness of observations'. Vigilance, therefore, stands for watchfulness, caution or circumspection.

Vigilance, as an eternal price for freedom, is taught even at childhood for whatever activities the child does. 'Be careful', is the watchword liberally tendered to any child when he indulges in any kind of activity. As the child grows up, he acquaints with the meaning of vigilance, which covers all aspects of human activity. One has to be vigilant when he goes for a walk on the road; one has to be vigilant while driving the vehicle; one has to be vigilant while making purchases in the grocery shops; one has to be vigilant while performing each and every household work. All these vigilant lessons are taught and learned in order to be productive and effective as well as for not being cheated or assaulted in any form by anybody. This principle of alertness and watchfulness applies to every activity that the human being undertakes. Therefore, it goes without saying that the same kind of alertness or watchfulness or caution or circumspection has to be applied when it comes to the performance at work place or profession. There may be `n' number of activities which one has to perform in the work place in the assigned job. All these jobs have to be performed with a same amount of prudence, which otherwise would have been shown for doing a domestic or personal work.

Therefore, the plain meaning of vigilance is to be vigilant. It is an absolute state of mind and a matter of pure common sense. In a slightly philosophical sense, it can be said; "not being vigilant and the awareness of being so, is in itself, is to be vigilant".

Nevertheless, like any other transformation, vigilance is not an exception and over a period of time, the meaning of vigilance had undergone a sea change transformation, and thereby making it a word to mean more than its meaning, at least in India.

Vigilance transformation

It is said that right from the colonial times, the presence of vigilance was being felt constantly in the guidelines and suggestions issued by higher authorities to those below to ensure administration and proper observance of the procedures and rules, as long as the government was governing. However, after the expansion of the activity of the government, the government servants were vested with vast authority and huge public funds were handled by them to fulfill the national objectives. The mounting aspirations, therefore, necessitated a formal system of check to ensure cleanliness in administration by preventing possible misuse of authority. Perhaps, at this juncture in the history of vigilance, the exact transformation on vigilance took place and the debut of vigilance as the mechanism to address the complaints of corruption against administration was made. Since then, there was no looking back and vigilance continues to be attached only with corruption and matters allied to it. In this process, the actual connotation of vigilance is lost sight of. This phenomenon is seen mainly in India and such a transformation of meaning for vigilance, perhaps, has not taken place in other countries, the way it happened in India.

Vigilance at present

"When the mystics showed the moon, the ignorant looked at the fingers", an old saying goes like this. This is what exactly has happened in the case of 'Vigilance". 'Vigilance' is seen as propriety of vigilance departments and vigilance officers. 'Vigilance' is not vigilance department, nor what all that vigilance department or vigilance officers do for that matter. The fact that the concept of so called vigilance departments and vigilance officers were evolved only to check whether everyone in his job, is performing his vigilance function or not, has been lost sight of.

As discussed earlier, vigilance is an integral part of every action that the human being does. It took so long a period for Vigilance to regain its recognition of being a function. In the recent times, Vigilance is being considered as a management function rather than a tool in the hands of the management. The issuance of Special Chapter on 'Vigilance Management in Public Sector Enterprises' by the Central Vigilance Commission in July 1999 is a proof for such recognition.

Vigilance, in the present context can be explained as follows:

"Vigilance need not be a dirty word associated always with investigation or enquiry, charge-sheets and punishments alone. It is not something that is apart, different, or alienated from the main organization or managerial effort. It is, in fact, an inalienable and integral part of management function. As a strong and unfailing blend with any management function, it can be a positive, constructive and catalytic influence by:-

(a) Raising storm signals regarding complexities or neglect of procedures

(b) Placing signposts for the path to purposeful and effective achievement of objectives

(c) Devising correctives and generally acting as a prophylactic agent

(d) Eliminating the corrupt and the crooked.

Vigilance as it actually mean, is an inherent part of any activity that is undertaken in the universe. Every individual in his own discipline has to ensure that a reasonable care is taken of his assets and resources and that they are not squandered away for other than legitimate work and rightful purposes. An incomplete perspective on this count would lead to undesirable result in the performing one's role. The quality circles (QCs) and the Total Quality Management (TQMs) are the recent jargons in the corporate world. The QCs and TQMs, in reality, call for eternal vigilance at all levels, in order to ensure that the systems and procedures laid down in the quality manuals are scrupulously followed. The checks and supervisions as stipulated in such quality manuals amounts to taking precaution or caution for carrying out the assigned duties and responsibilities within the frameworks of the organization, which perhaps, in a broader sense is termed as Vigilance. These concepts have been accepted and well recognized without knowing the fact that what operates such concept is nothing but eternal vigilance.

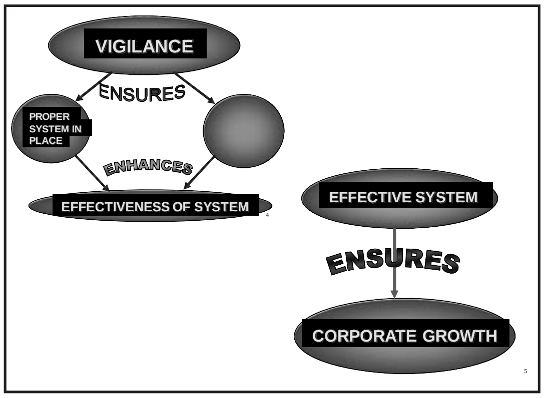
While policing is intended to catch those who do wrong things the vigilance function is to catch those who are doing the things wrongly, intentionally. While the job of policing is not to catch someone who does good things, it is the job of vigilance function to catch someone doing right things. Every individual can do this function and catch himself or herself for doing things rightly or wrongly and then others too.

Therefore, vigilance is a function. It is a core management function to be performed by everyone simultaneously along with every other function that one performs.

(iii) Interface between Corporate Governance and vigilance

Operating internal controls

The interface between corporate governance and vigilance is the internal controls through the systems. As discussed earlier, systems are nothing but the combination of rules, regulations and procedures. Having such system in a corporation is not sufficient but following such a devised system is more important to see the results. Vigilance as a function, by each individual, ensures that not only the systems are in place, but also they are followed to see the corporate growth, as may be seen below:



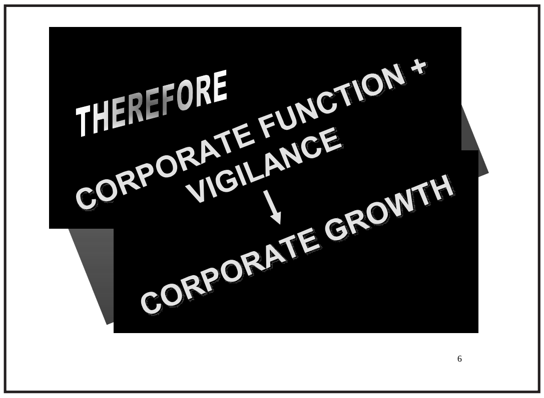
The failure on the part of individual to perform the function of vigilance invites intervention of the so-called vigilance officers or the vigilance department. Avoidance of such failures and effective performance of such vigilance function alone, in the corporate world is called as corporate governance. Therefore, corporate governance is operated through the operating system, which is none other than Vigilance. As in the computer every software runs only on the operating system, likewise, in performing every function in the corporate world, may it be managerial or by the board or by anybody for that matter, it has to be performed only with vigilance as the operating system. That is what all that corporate governance means.

When it comes to PSEs in particular, one has to perform the vigilance function meticulously before performing other functions because it is ultimately the public money, which is being handled. In the case of private sector also, of course, it is the shareholders money and thus the same amount of vigilance is required. It is not out of place to mention that in the recent times, the concept of vigilance has also been recognized by the private sectors too. A recent advertisement by one of the Reliance group of companies, namely, BSES for the recruitment of professionals for 'Vigilance' is one such example. This is one of the factors, which support the thesis that corporate governance operates on vigilance.

To sum up

Whenever vigilance is talked about, only the vigilance as a function should come to the mind rather than the vigilance department or vigilance officers for that matter. The job of the so-called vigilance department is to ensure whether such vigilance function is performed or are being performed diligently by everyone at every level and at all stages of the business. The so-called vigilance officers come in to picture only when there is a failure in performing the vigilance function. Thus the exact role of vigilance department is that of a 'watch dog'. Therefore, one has to perform the vigilance function even in the absence of vigilance department. That is what one does at home.

Let there be systems and procedures. Let them be followable. If not, let them be amended from time to time on a real time basis, as required. Let there be a meticulous observance of systems and procedures at all stages. Let there be a common prudence and alertness prevail while following the systems and procedures. There lies the vigilance function. Therefore, any corporate function is operated along with the vigilance function is destined for corporate growth and that is what is expected of from good corporate governance.



It is, therefore, in the proper admixture of every management function and vigilance function in right perspective, lies the path for good corporate governance. This admixture is nothing but the compatibility of the software (corporate governance) and the operating system (vigilance). That is how vigilance helps in the good corporate governance as the operating system. Ultimately, the fact remains that eternal vigilance ought to be the essential ingredient for good corporate governance. After all, as Shri N. Vittal [13] said, it is the principle of enlightened self-interest, the basic ***dharma*** of the corporate world, which paved the way for the current trend of good corporate governance.

(The author is the Founder of SIV-G (Self Imposed Vigilance for Good Governance) – www.siv-g.org. This article was first published in 2003 in the Journal Vigilance Professional, published by Dr. S. Subramanian, IPS(Retd), Founder, Patron, Vigilance Study Circle)

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"Always do right. This will gratify some people, and astonish the rest."

Mark Twain (1835–1910), US writer
Source : Speech to the Young People's Society, Greenpoint Baptist Church, Brooklyn, New York (1901)

CORPORATIONS: NEED FOR CONSCIENTIOUS MEN THAN CONSCIENCE

Alok Kumar Gupta & Saurav Bhaumik[1]

INTRODUCTION

Henry David Thoreau once said, "It is truly enough said that a corporation has no conscience. But a corporation of conscientious men is a corporation with conscience."[2]

Almost all the countries have been struggling to ensure good corporate governance in their countries so that the rights and property of shareholders and other stakeholders of the corporation are protected, secured and kept intact. This is primarily because the directors of the corporations are considered to be their trustees. The stockholders also have a joint interest in all the property and effects of the corporation.[3] Moreover under the general principles of equity the stockholders always have a legal remedy against the damages which they may sustain by a fraudulent breach of trust.[4] Accordingly there have been both legal and institutional response to the problem of corporate misgovernance[5], but in vain, with each new set of legal and institutional remedies another kind of corporate fraud surface thereby making the investors and stakeholders[6] lose their lifetime earnings. India is no exception to this rule. There had been persistent corporate frauds in India which has tarnished and corroded the image of the Indian corporate sector. The failure of the legal framework can be attributed to the fact that law often lacks the necessary flexibility to adjust to and permeate dynamic business organizations.[7] Extensive research had also revealed that the complex legal compliance programs often exist only to protect the top management from blame.[8] This is inevitably acting as an impediment in the free flow of international investments in the Indian market.[9] The objective of the present paper is to give a philosophical and ethical discourse to the aforementioned malady.

DEFINING CORPORATE GOVERNANCE

The Organization for Economic Co-operation and Development offers what has become the globally accepted definition of corporate governance. "Corporate Governance is the system by which business corporations are directed 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 on corporate affairs."

Addressing the students of the George Washington University in 2006, Infosys Technologies founder N R Narayana Murthy stated what corporate governance meant to him: "Corporate governance, to me, is about maximising shareholder value legally, ethically and on a sustainable basis, while ensuring fairness to every stakeholder which entails the company's customers, employees, investors, vendor-partners, the government of the land and the community. Corporate governance development has consequently become a major policy priority not only in developing economies but also in developed economies. Most of the initiatives are modelled after measures recommended in or adopted by the mature market economies that have been pioneers in corporate governance development.[10]

Recently there have been escalating theoretical developments in the convergence of Corporate Social Responsibility[11] and Corporate Governance, keeping in purview the exponential number of corporate frauds. Corporate Social Responsibility seeks improved behaviour from corporations. It asks corporations to broaden relationships with multiple stakeholders, engage in meaningful and sustained efforts to improve communities and to reform societal rules especially those embodied in both law and ethical custom.[12] This is principally because companies serve a wider range of human values apart from its sole focus on economic values.[13]

CORPORATE GOVERNANCE: THE DYNAMICS

The public and academic discourse on corporate governance commenced since 1990s after the unexpected collapse of giant corporations like Enron[14], Worldcom, Adelphia, Global Crossing, etc. in USA and also in many other countries. These scandals have all contributed to a growing distrust of business and further eroded public trust. The idea of corporate governance is a very critical topic of research because some of the corporate systems are large enough to be termed as systems of government.[15] Hence, there is a duality of corporate and political governance, in other words Corporate Governance is merely an analogue of political governance.[16] There are several large corporate entities which play a gargantuan role in developing a civilization and are inextricably linked to the life of each and every individual in the society. It indirectly forms a virtual economic framework of governance. Thus if corporate hegemony is not regulated by ethical principles it would inadvertently result in an insidious plague virtually crippling the whole societal structure. The ethical regulation of corporations should essentially revolve around the structure and functioning of the board and its relations with other corporate organs *vis a vis* the purpose of maximising profits.[17] Thus the issue of ethical leadership should have to be coextensively dealt within its complex capitalistic framework.

CORPORATE GOVERNANCE: THE MEASURES

The first and foremost duty of a corporation is to manage its own affairs properly and profitably. That is the greatest service it can perform. A corporation has a duty to compensate its employees and reward its investors to the best of its ability. It has a duty to create favourable working conditions and to produce goods and services that meet the highest tests of safety and reliability.[18] Efficient governance could also be achieved by strengthening the accountability of corporate executives to their boards and their shareholders.

The growing incidence of misgovernance in the corporate world led to the setting up of Cadbury Committee, Greenbury Committee, Hampel Committee etc. The core objective of all of these committees was to go in to the causes of corporate corruption and frauds and suggest remedial measures that may minimize and mitigate such incidents.

THE INDIAN CONTEXT

The protection of public interest is the preservation of a stable society.[19] India entered into an era of massive liberalization of its economy in the early 1990s to integrate its market with the world market and to carve out a space for itself within the larger ambit of globalization. This also led to the growth of corporate world and hence the consequent growth of capital market. The 1990s saw hordes of new investors being drawn into the stock markets, but also a series of corporate and financial scams like the Harshad Mehta securities scam of 1992, as also the numerous obscure companies that went public, collected crores of shareholder money and disappeared, which eventually shook the very basis of investor confidence in India. The fallout of these scams affected millions of investors across the country, causing widespread public dismay. The persistent high profile corporate governance failures in developed and developing countries[20], have eventually brought the subject to media attention. The issue is particularly important in developing countries like India since it is central to financial and economic development.

With the unprecedented boom of corporate in India, the nature of corporate fraud also went on changing and was ever growing. Consequently, number of legal and institutional responses were conceived and implemented to check such unethical wrong doings by the corporate. Confederation of Indian Industry (CII) set up a committee chaired by Rahul Bajaj in 1996 which developed India's first voluntary code of corporate governance for listed companies. Later the Securities and Exchange Board of India (SEBI) constituted two committees to look into the issue, the first chaired by Kumar Mangalam Birla which submitted its report in early 2000, and the second was chaired by Narayana Murthy which submitted its report three years later. These three committees together were instrumental in bringing about far reaching changes in corporate governance in India through the formulation of clause 49 of the Listing Agreement. Concurrent with these the Department of Company Affairs of the Ministry of Finance too began contemplating improvements in corporate governance.

Developments were introduced in the statutory framework as well. The Companies Act of 1956 mandates corporate law in India and provides the second pillar, the first being clause 49, of the corporate governance edifice. Clause 49 of SEBI's Listing Agreement outlines the mandatory requirements for publicly held companies. By and large, the provisions of clause 49 closely resemble those of the Sarbanes-Oxley measures in the United States of America, but the aforesaid regulations went in vain with the emergence of the Satyam Scam.

The Satyam saga was the ultimate exemplar of corporate misgovernance in the country. Moreover, long before Satyam's politically influential chairman's confession, the shareholders had expressed dissatisfaction with Ramalinga Raju's leadership. Many of them also alleged that the board of directors and its members failed to meet their basic responsibilities.[21] Eventually B. Ramalinga Raju announced confession of over Rs 7800 crore financial fraud and resigned as the Chairman of Satyam. He revealed in his letter that his attempt to buy Maytas Companies was his last attempt to "fill fictitious assets to real ones."[22]

Research had revealed that the investors had to raise their voice to prevent the Raju brothers from using their dominant position to benefit their family business instead of the Satyam Shareholders.[23]

THE PROBLEM

The stories of corporate scams and the corporate peccadilloes are regular norms of the corporate India and perhaps the corporate world. As mentioned-above there has been number of institutional and legal responses to contain the problem. Therefore, it can be contemplated that there is a serious lack of conscientious men at the topmost level of the corporations. Lack of conscientious men at the helm of the corporate superstructure would inexorably lead to serious issues of corporate misgovernance notwithstanding the fact that the corporations are protected by legal and institutional framework. A system of concentrated ownership[24] would continue to flourish where the legal regime is unable to guarantee an adequate protection to the rights of the minority shareholders.[25] Heath and Norman had also put forward the idea that the source to most of the biggest corporate scandals can be traced to the breakdown of the governance relation between shareholders, the board and the senior executives.[26]

The most consistent common element across all these companies is the involvement of senior management in the frauds including members of the Board of Directors, the CEO, the CFO, and other key executives.[27] Moreover Corporate executives are neither elected representatives of the people nor are they anointed or appointed as social guardians. They therefore lack the social mandate of those who would pursue ethically or socially motivated policies.[28] Thus reverting back to the proposition put forward by Thoreau we can argue that the people at the helm of affairs should be mended, in other words there is a dire need for a paradigm shift in the notion of an efficient corporate leader. Certain fundamental structural changes in the ethical framework of the higher level of the corporate ladder are required. Most essentially the traditional notion of an ethical corporate leader should be deconstructed as it has repeatedly resulted in big corporate frauds. Corporate Leaders should be an embodiment of the purpose and values of the organization and should essentially be moulded with the virtue of ethics.[29] The corporate leaders should imbibe the dynamics of morality which is prevalent in their ethical environment. Michael Pickett had developed the idea that the operation of an organization primarily emanates from the various propensities for moral climates which is virtually the by-product of the ethical environment.[30] The ethical environment is very crucial for any corporate decision because the values of the corporate leaders often turn out to be a poor guidepost. This is because individualistic corporate decisions void the ethical environment often fails to serve as a beacon for the body corporate.

The corporate leaders should inculcate the "Categorical Imperative" which connotes the dictate of moral practical reason within their moral framework.[31] A corporation run by irresponsible managers will be an irresponsible corporation.[32] This is primarily because a corporation is not moralistic by nature; it is pragmatic, and is largely dependent on the actions of the persons who are at the topmost position of the corporation. It had been observed by researchers that big corporations can neither regulate themselves, nor check their own greed, self-interest and opportunism[33], which is indirectly the by-product of the lack of conscientious people at the helm of affairs of the corporation.[34] Thus institutional and legal regulations fail to succeed where profit and self enrichment becomes the sole driving forces behind any corporate entity which is a by-product of unrestrained capitalism.[35] The aforesaid contention can be attributed to the fact that the self regulating norms and the introduction of regulatory bodies and various reformist measures within the legal labyrinth have failed to ensure that corporations and CEOs serve wider interests than their own.

Unrestrained capitalism can be an essential driving force behind the large scale corporate frauds. The consequences have not only led to immense financial and non financial ramifications but also blatant ethical lapses. Thus compliance to ethical practices would be the only method to curb the endemic financial corruption within the corporations. This would include educating the board of directors about their legal and ethical responsibilities and also about the penalties which would result from the breach.[36]

Hence, reconstructing Thoreau's view we can infer that the wisdom that comes to the individual is far more superior to the wisdom which he inculcates through the realms of political power or any supreme authority(the corporation in this case because the notion of corporation is coextensive with that of the State). Men are not born with impeccable social credentials. These credentials or intentions have to be nurtured and it requires the will to do good. Thus it is desirable to cultivate a respect for law and morality within the corporate which would inevitably catalyse in the booming of conscience[37] within the body corporate. The American Law Institute comments on this issue by saying that 'where conflict exists between ethical considerations and corporate profitability, the most desirable and appropriate course would be to comply with the ethical considerations even though this would not enhance corporate profit or shareholder gain.[38] A conscious business generally promotes mindfulness for all its stakeholders. Without conscious employees, companies cannot achieve greatness, or even survival. Unconscious employees do the opposite. They blame others for problems, seek immediate gratification regardless of ethics, and claim to always be right. They hide significant information, sweep conflicts under the table and negotiate to beat their opponents. They expect to get what they need without asking, make irresponsible promises, and fail to diligently undertake their commitments. To attract conscious employee managers must exercise conscious leadership.

The most important fiduciary duty[39] that a director owes is the duty to act bonafide and in the interest of the Company, i.e. the duty of loyalty.[40] Each employee must work to provide value for the customers.[41] Goopaster and Mathews had revealed that higher percentage of directors from outside in the board of directors increases its effectiveness as a monitor of management.[42] Corporations are not persons. They are artificial legal constructions, machines for mobilizing economic investments towards the efficient production of goods and services. Thus from the aforesaid contention we can conclude that corporation are not responsible for the fraudulent endeavours, but the individuals responsible behind such endeavours should face the liability.[43] With that shift in emphasis, corporate ethics[44] would become a necessity, rather than a luxury for which it was too often mistaken, in both the corporation and the society at large. The notion of corporate leadership needs to be redefined. Leaders should demonstrate a higher order self discipline in their dealings, even as they took higher order risks to insure the well-being of those they led.[45] There is also a need for a participatory interdependent dynamic environment between governments, businesses and non profit organizations that come together to plug gaps the others may not be able to fill.[46]

CONCLUSION

Good Corporate Governance could be achieved through two ways: one by more and more of legal and institutional response i.e. by creating more laws and institutions; secondly, through minimizing the role of laws and institutions and maximizing the role of men at the helm of affairs i.e. such men should engineered in a manner that they do business with conscience. N R Narayana Murthy in his book, "A Better India, A Better World", has rightly mentioned that Corporations are best run with simple business rules. Simple business rules are easy to understand, easy to follow, and easy to communicate. The scope for cheating is drastically reduced or may stand mitigated when there are simple rules. A corporate or a government when formulate rules should ask themselves if they are being fair to all the constituents? Indeed, 'the softest pillow is a clear conscience'.

Business ethics are applied ethics. It is the application of our understanding of what is good and right to that assortment of institutions, technologies, transactions, activities and pursuits that we call business. Thus, a student of business ethics would ask for a framework of basic principles for understanding what is meant by good and right; only then can one proceed to profitably discuss the implications these have for the business world. However, business or corporate ethics, today remains confined to classroom discussion and debate, academic discourse, and in mere words in widely discussed book. Sometimes, such principles also make inroads into the board room where the smartest guys of business world make policies and decisions.

Therefore, the need of the hour is conscientious men in the business world and the corporate shall come to have conscience automatically. When the corporate develop conscience the corporate frauds shall reduced to a thing of the past. Therefore, the need of the hour is to engineer or nurture the nature of men at the helm of affairs rather than evolving another piece of legislation or an impeccable corporate like institution to contain the misgovernance within the corporate.

(Footnotes)

1 Alok Kumar Gupta is Professor and Dean at National University of Study and Research in Law, Ranchi and Saurabh Bhaumik is a third year student of Law at the same University.

2 Henry David Thoreau, "Civil Disobedience" (Hayes Barton Press 2005), p.3.

3 In Dodge v. Ford Motor Co., 170 N.W.668,684(Mich.1919) the Hon'ble Court observed that a business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end and does not extend to a change in the end itself, to the reduction of profits or to the non distribution of profits among shareholders in order to devote them to other purposes.

4 Brian McCall, "The Corporation as Imperfect Society", 36 *Delaware Journal of Corporate Law*. 509, (2011), p.1.

5 Sarbanes Oxley Act, 2002.

6 Freeman gave a very interesting idea of the stakeholder theory. He contends that stakeholders themselves and their activities are very important to be taken into the management of companies. He states "Stakeholders may bring an action against the directors for failure to perform the required duty of care." *See* Tony Ike Nwanji and Kerry E.Howell, "The Stakeholder Theory in the Modern Global Business Environment", 1 *International Journal of Applied Institutional Governance*. 1, p.3.

7 Sally S. Simpson, "Corporate Crime, Law and Social Control" (Cambridge University Press 2005), p.5.

8 Surendra Arjoon, "Corporate Governance:An Ethical perspective", p.8, *available at* http://sta.uwi.edu/conferences/financeconference/Conference%20Papers/Session%205/Corporate%20Governance%20-%20An%20Ethical%20Perspective.pdf

9 Elisabetta Basilico et al., "Asia's Enron: Satyam (Sankskrit Word for truth)", 4 *Journal of Forensic & Investigative Accounting*. 2, (2012), p.151.

10 Cyril Lin, "Public Vices in Public Places: Challenges in Corporate Governance Development in China", p.2, *available at* http://www.oecd.org/dataoecd/7/26/1931396.pdf

11 Corporate Social Responsibility is often viewed as an industry or corporation based concept with some base in law, but it is largely concerned with preserving the public face of the corporation. However, in recent years, the focus of Corporate Social responsibility gas shifted to new areas ranging from environmental protection to sustainable development and labour concerns. *See* Alexandra R. Harrington, "Protecting workers' rights in a post wisconsin world: strategies for

organizing and action in an era of diminished resources and embattled unions:corporate social responsibility, globalization, the multinational corporation, and labour: an unlikely alliance", 75 *Albany Law Review*. 483, (2011), p.1.

12 Michael B.Runnels et al., "Corporate Social Responsibility and the New Governance : In search of Epstein's Good Company in the Employment Context", 43 *Akron Law Review*. 501, (2010), p.19.

13 Manuel Castelo Branco and Lucia Lima Rodrigues, "Positioning Stakeholder Theory within the Debate of Corporate Social Responsibility", 12 *Electronic Journal of Business Ethics and Organization studies*. 1, (2007), p.12.

14 Disclosures of self dealing transactions in the fall of 2001 seriously destabilized Enron. The disclosures concerned a complex of side deals involving two limited partnerships of which Enron's CFO, Andrew Fastow, was the manager of the general partner. These arrangements put $30 million into Fastow's pocket, and resulted in an overstatement of Enron's earnings over four years of at least $591 million. *See* William W. Bratton, "Enron and the Darker Side of Shareholder Value", 76 *Tulane Law Review*. 1276, (2002), p.1305.

15 Brian McCall, "The Corporation as Imperfect Society", 36 *Delaware Journal of Corporate Law*. 509, (2011), p.1. *See also* Stephen Bottomley's idea of corporate constitutionalism. *available at* Angus Corbett and Peta Spender, "Corporate Constitutionalism", 31(1) *SydneyLaw Review*. 147, (2009), p.6.

16 Cyril Lin, "Public Vices in Public Places:Challenges in Corporate Governance Development in China", p.2, *available at* http://www.oecd.org/dataoecd/7/26/1931396.pdf

17 Amiram Gill, "Corporate Governance as Social Responsibility:A Research Agenda", 26 *Berkeley Journal of International Law*. 2, (2008), p.456.

18 Harold Burson, "Social Responsibility or Telescopic Philanthropy :The Choice is ours", (1973), p.2, *available at* http://www.bursonmarsteller.com/Innovation_and_insightsblogs_and_podcasts/harold_burson_blog/Documents/1973-03-20%20Columbia%20UniversityGarrett%20Lecture.pdf

19 Ghanshyam Shah, "Social Justice" (Rawat Publications 1998), p.142.

20 Anti Social Financial Practices are a regular occurrence in both developed and developing countries, and the corporate executives have played a key role in facilitating capital accumulation by the elite. *See* Choo and Tan, "An 'American Dream' Theory of corporate Executive Fraud", 31 *Accounting Forum*, (2007), pp.203-215.

21 MarkJ.Epstein, "Challenges of Governing Globally", (October-2010), p.28, *available at* http://www.imanet.org/PDFs/Public/SF/2012_07/07_2012_epstein.pdf,Strategic

22 J.S.Sharma, "What went wrong with Satyam", p.2. *available at* http://www.iodonline.com/ArticlesInst%20of%20DirectorsWCFCG%20Global%20CoventionPaper%20Prof%20J%20P%20SharmaWhat%20Went%20Wrong%20With%20Satyam%20new.pdf

23 Elisabetta Basilico et al., "Asia's Enron:Satyam(Sankskrit Word for truth)", 4 *Journal of Forensic & Investigative Accounting*. 2, (2012), p.151.

24 Characterised by controlling blockholders, weak securities markets, high private benefits of control and low disclosure and market transparency standards, with only a modest role played by the market for corporate control. *see generally* David Hahn, "Concentrated ownership and control of corporate reorganizations", (Working Paper no.6-03, 2003), *available at* http://www.biu.ac.il/law/unger/working_papers/6-03.pdf

25 Robert Cobbaut and Jacques Lenoble, "Corporate Governance: An Institutionalist Approach" (Kluwer Law International 2003), p.31.

26 Joseph Heath and Wayne Norman, "Stakeholder Theory, Corporate Governance and Public Management:What can the history of state-run enterprises teach us in the post-Enron era?", 53 Journal of Business Ethics, (2004), p.266.

27 Howard Rockness and Joanne Rockness, "Legislated Ethics: From Enron to Sarbanes Oxley, the Impact on Corporate America", 57 *Journal of Business Ethics, (*2005), p.35.

28 Keneth E.Goopaster and John B. Mathews Jr , "Can a Corporation Have a Conscience", 60 *Harvard Business Review*, (1982), pp. 132-141.

29 This is primarily because a Corporate Leader is inevitably the most powerful individual in the whole system of power around the organization. *See* Hatice Uzun et al., "Board Composition and Corporate Fraud", 60 *Financial Analysts Journal*. 3, (2004), pp33-43.

30 MichaelC.Pickett, "UnderstandingEthicalLeadership", p.50, *available at* http://www.asbbs.org/files/2005/PDF/Pickett.pdf

31 B. Sharon Byrd and Joachim Hruschka, "Kant's Doctrine of Right: A Commentary" (Cambridge University Press 2011), p.282.

32 Troll Covey, "The Ethics of Open Access to Research: A Call for Civil Disobedience and Moral Courage", (Library Research and Publications, Paper 79, 2009), p.3.

33 The personal self interests of the corporate executives often conflate with the shareholder interests which gives rise to

complex agency issues. *See* Donaldson et al., "Towards a Stewardship Theory of Management", *The Academy of Management Review*. 22, (1997), p.15.

34 In pursuit of corporate profits and personal financial interests, the corporate CEOs have engaged in anti social financial practices such as bribery and corruption. However, an emerging body of literature have argued that bank corporate executives have been increasingly using their expertise to conceal and promote anti social financial practices. *See* Julius Olatunde Otunsnaya, "An Investigation of Corporate Executive Fraud by CEOs in theNigerian Banking sector", p.5, *available at* http://www.organizzazione.unina.it/cms7/proceedings/proceedings_stream_33/Otusanya.pdf

35 Maximizing profits was not among the top priorities of corporate law in the early period. The restrictions and conditions imposed on corporations, discussed above, make this quite clear. *see generally* P.M.Vasudev, "Corporate Law and its efficiency: A review of History", 50 *American Journal of legal history*. 237, (2010), p.5.

36 In order to motivate independent directors to carry out their responsibilities, their liabilities must be made credible so that those who fail to exercise due diligence have to take serious financial restitution. Ultimately, India will have to develop a business culture in which directors know what is expected of them and are motivated to carry out due diligence. *See* Ajay Rajan and Suman Pahal, "The Achilles Heel of Indian Corporate Governance System", 2 *Zenith International Journal of Business Economics & Management Research*. 7, (2012), p.186.

37 Conscience does not denote a psychological phenomenon but instead is practical reason, confronting the human being with his duty whenever a law is applicable. *See* B. Sharon Byrd and Joachim Hruschka, "Kant's Doctrine of Right:A Commentary" (Cambridge University Press 2011), p.284.

38 Shelly D. Green, "Defending the 'Time Culture': The Public and Private Interests of Media corporations", 43 *Federal Communications Law Journal*, pp.1990-1991.

39 Fiduciary duties are the duties that have been entrusted to someone to perform only for the entrusters. Of the fiduciary duties, the most fundamental ones are "the duty of loyalty," "the duty of care," and "accountability." *See* Ryuuichiro Kurihama, "Corporate Social Responsibility, Corporate Governance and Auditing in Japan", p.9, *available at* http://www.iae.univ-poitiers.fr/EURO-ASIE/Docs/Asia-in-Extenso-RKurihamamars2005.pdf

40 *See* Dale & Carrington P.Ltd v. P.K.Prathapan , 122 Comp Case 161(SC) where the Hon'ble Supreme Court of India held that the fiduciary capacity within which the directors have to act enjoins them a duty to act on behalf of a company with utmost good faith, utmost care and skill and due diligence and in the interest of the company they represent. They have a duty to make full and honest disclosure to the shareholders regarding all important matters relating to the Company.

41 R.Edward Freeman and Lisa Stewart, "Developing Ethical Leadership", (2006), p.3, *available at* http://www.corporate-ethics.org/pdf/ethical_leadership.pdf

42 James R. Booth et al., "Board of Directors, Ownership and Regulation", 26 *Journal of Banking & Finance*, (2002), pp.1973-1996.

43 Keneth E. Goopaster and John B. Mathews Jr, "Can a Corporation Have a Conscience", 60 *Harvard Business Review*, (1982), pp.132-141.

44 Ethics is concerned with right and wrong .It discerns good from bad behaviour based on principles of conduct grounded in moral values, duty and obligation. *see generally* Troll Covey, Denise, "The Ethics of Open Access to Research: A Call for Civil Disobedience and Moral Courage", (Library Research and Publications, Paper 79), (2009), p.3.

45 Leigh Hafrey and Cate Reavis, "Corporate Personhood, Business Leadership, and the U.S. Presidential Election of 2012", p.9, *available at* https://mitsloan.mit.edu/MSTIR/Leadership/CorporatePersonhood/Documents/11134%20Corporate%20Personhood%20Business%20Leadership%20and%20the%20U%20S%20%20Presidential%20Election%20of%202012%20FINAL.pdf

46 Breena E. Coates, "Leadership Driven Conscious Capitalism and the triple bottom line", p.3, *available at* http://www.aabri.com/LV11Manuscripts/LV11107.pdf

"You can't learn too soon that the most useful thing about a principle is that it can always be sacrificed to expediency."

W. Somerset Maugham (1874–1965), British novelist, short-story writer, and dramatist.
Source : *The Circle* (1921)

Indexes based on Corporate Governance : Review of Practices

The World Bank's corporate governance assessments reveal growing awareness around the world of the importance of corporate governance. Almost all the countries assessed are undertaking reforms to bring their legal and regulatory frameworks into compliance with the Organization for Economic Co-operation and Development's (OECD) principles of corporate governance. Quantifying the risk of corporate governance across international markets has also posed a challenge for investors trying to deal with the issue. Setting up of corporate governance indexes and exchanges would be such a reform. This not only provides natural incentive to companies complying with good corporate governance but also provides a platform for small and medium sized enterprises.

Below mentioned are some of the major indexes observing corporate governance as the threshold for its listings:

Novo Mercado

In 2001, BOVESPA, the Sau Paulo Stock Exchange launched Novo Mercado, a separate listing segment for companies that adhere to good corporate governance. It accounts for almost 15% of the number of companies traded in Brazil, and contributes 43% of the market capitalization, and has out-performed the general market index by more than 100% since June, 2001.

It is a special listing segment that demands timely compliance to the set of rules and laws that are more than what is required by any other listings. The establishment of Novo Mercado promotes socially responsible business community and fosters growth in the Brazilian market. The stock exchange is reserved only for well governed companies and organizations promoting interests of minority shareholders and adoption of ethics and values in the business community.

Listing in Nova Mercado requires the following:

- Public share offerings have to use mechanisms to favor capital dispersion and broader retail access.
- Maintenance of a minimum free float, equivalent to 25% of the capital.
- Same conditions provided to majority shareholders in the disposal of the Company's Control will have to be extended to all shareholders.
- Establishment of a two-year unified mandate for the entire Board of Directors, which must have five members at least, of which at least 20% (twenty percent) shall be Independent Members.
- Disclosure of annual balance sheet, according to standards of the US GAAP or IFRS.
- Improvements in quarterly reports, such as the requirement of consolidated financial statements and special audit revision.
- Obligation to hold a tender offer by the economic value criteria, in case of delisting or cancellation of registration as publicly-held company.
- Compliance with disclosure rules in trades involving securities issued by the company in the name of controlling shareholders.
- Some of these obligations must be approved at the General Shareholders Meetings and included in the corporate bylaws

These listing regulation help increase shareholder's rights and enhance the quality of information commonly disclosed by companies. Additionally, the Market Arbitration Panel for conflict resolution between investors and companies offers a safer, faster and specialized alternative to investors.

Apart from this, BOVESPA has also designed Special Corporate Governance Levels; Level 1 and Level 2, based on the conduct of companies, managers and controlling shareholders considered as important for valuation of shares and other assets issued by the company. 169

FTSE ISS Corporate Governance Index

FTSE is an independent company owned by The Financial Times and the London Stock Exchange. FTSE indices are used extensively by investors world-wide such as consultants, asset owners, asset managers, investment banks, stock exchanges and Brokers. The FTSE ISS Corporate Governance Index is a collaboration of FTSE and Institutional Shareholder Services (ISS), the premier corporate governance ratings agency.

The FTSE ISS Corporate Governance Index is a series based on the companies which have good corporate governance record. It comprises of six regional and country equity indices covering 24 developed countries as defined by the FTSE Global Equity Index Series. The underlying idea is to assist investors by rating the performance of the companies on the basis of its corporate governance practices.

The index is primarily managed and constantly reviewed by the FTSE Index Board. The Advisory committee supports the Index by determining the listing criteria.

FTSE ISS Corporate Governance Rating is mainly derived on the basis of the below mentioned five governance themes:

- Board structure and independence: The composition and processes of the board and the structure of key standing committee are examined.

- Equity Structure: This involves evaluation of the company's capital structure and existing anti takeover devices.

- Compensation system for executive and non executive directors: This involves evaluation of the existing rewarding schemes and practices for directors.

- Independence and integrity of the audit process: This evaluates the composition of the audit committee and the audit process.

- Executive and non-executive stock ownership: The balance between the ownership and shareholder interests is measured.

The FTSE ISS Corporate Governance Indices includes the following:

- FTSE ISS Developed Corporate Governance Index

- FTSE ISS Europe Corporate Governance Index

- FTSE ISS Euro Corporate Governance Index

- FTSE ISS Japan Corporate Governance Index

- FTSE ISS UK Corporate Governance Index

- FTSE ISS US Corporate Governance Index

Governance Metrics International

Governance Metrics International (GMI) is an independent rating and research agency founded in April 2002. It analyzes the corporate governance practices of publicly traded companies. It prepares exhaustive reports and rates the company's overall governance profile on the basis of its Board Accountability, Financial Disclosure and Internal controls, Shareholder rights, Executive compensation, Market for control and Ownership Base and Corporate Behavior and CSR Issues. All companies on the GMI list are re-rated and reviewed on a quarterly basis GMI Ratings are extensively used by corporations, law and accounting firms, proxy solicitors, insurance underwriters, central banks, regulatory agencies and other institutional investors and fund managers.

Apart from rating and research, GMI is also engaged in providing advisory services on corporate governance issues to a diverse client base including stock exchanges, regulatory bodies and other institutional investors.

Conclusion

Corporate Governance indexes are helping the investors seeking devices that fulfill their demand for good governance. It was even revealed in a study that investors are ready to pay 18% more for shares of a well governed company.

Moreover, well managed and governed companies are outpacing other companies in getting investments especially after scams like ENRON. However, the value for good governance is never immediate. But it definitely ensures long term profitability.

(Source: Corporate Governance : Review of Practices http://www.nfcgindia.org/pdf/corporate_governance_report.pdf)

"If it is not right, don't do it; if it is not true, don't say it."

John A. Byrne, US
Source : *Fast Company : The Rules of Business* (2005)

"Be the master of your will but the servant of your conscience."

Robin S. Sharma (1965–), Canadian self-help writer.
Source : *MegaLiving!: 30 Days to a Perfect Life* (1995)

Ethical Theories and Corporate Governance

Saswati Pritispada Mohapatra[1]

There are ethical theories that can be closely associated to corporate governance. These include business ethics theory, virtue ethics theory, feminist ethics theory, discourse ethics theory, postmodern ethics theory.[2]

- Business ethics is a study of business activities, decisions and situations where the right and wrongs are addressed. The main reasons for this are the power and influence of business in any given society is stronger than ever before. Businesses have become a major provider to the society, in terms of jobs, products and services. Business collapse has a greater impact on society than ever before and the demands placed by the firm's stakeholders are more complex and challenging. Only a handful of business giants have had any formal education on business ethics but there seems to be more compromises these days. Business ethics helps us to identify benefits and problems associated with ethical issues within the firm and business ethics is important as it gives us a new light into present and traditional view of ethics. In understanding the 'right and wrongs' in business ethics,[3] injected morality that is concerned with the norms, values and beliefs fixed in the social process which helps right and wrong for an individual or social community. Thus ethics is defined as the study of morality and the application of reason which sheds light on rules and principle, which is called ethical theories that ascertains the right and wrong for a situation.

- Feminist Ethics-Whilst business ethics theory focuses on the "rights and wrongs' in business, f*eminist ethics theory* emphasizes on empathy, healthy social relationship, loving care for each other and the avoidance of harm. In an organization, to care for one another is a social concern and not merely a profit centered motive. Ethics has also to be seen in the light of the environment in which it is exercised. This is important as an organization is a network of actions, hence influencing trans-communal levels and interactions.[4]

- Discourse Ethics- On the other end, *discourse ethics theory* is concerned with peaceful settlement of conflicts. Discourse ethics, also called argumentation ethics, refers to a type of argument that tries to establish ethical truths by investigating the presuppositions of discourse.[5] It is contended that such kind of settlement would be beneficial to promote cultural rationality and cultivate openness.

- Virtue ethics theory- Focuses on moral excellence, goodness, chastity and good character. Virtue is a state to act in a given situation. It is not a habit as a habit can be mindless.[6] Aristotle calls it as disposition with choice or decision. E.g.- if a board member decides to be honest, now that a decision which he makes and thus strengthens his virtue of honesty.

- Lastly, postmodern ethics theory goes beyond the facial value of morality and address the inner feelings and 'gut feelings' of a situation. It provides a more holistic approach in which firms may make goals achievement as their priority, foregoing or having a minimal focus on values, hence having a long term detrimental effect. On the other hand, there are firms today who are so value driven that their values become their ultimate goal.[7]

(Footnotes)

1 Saswati Pritispada Mohapatra is a student of Third Year BA(Hons.)LLB(Hons.) at National University of Study and Research in Law, Ranchi.

2 '*Fundamentals and Ethics Theories of Corporate Governance'* in www.eurojournals.com

3 Survey conducted by Crane and Mattern in 2007.

4 Study by Casey in 2006.

5 Academically, This Theory was proposed by Habermas in 1996 and by Meisenbach in 2006.

6 Recommended by Annas in 2003 in Fundamental and ethic theories of Governance.

7 By Balsubramanium in 1999 in Fundamental and ethic theories of Corporate Governance.

Accountability breeds response-ability.
Stephen R. Covey

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