Corporate governance refers to the set of systems, principles and processes by which a company is governed. They provide the guidelines as to how the company can be directed or controlled such that it can fulfill its goals and objectives in a manner that adds to the value of the company and is also beneficial for all stakeholders in the long term. Stakeholders in this case would include everyone ranging from the board of directors, management, shareholders to customers, employees and society. The management of the company hence assumes the role of a trustee for all the others.

What are the principles underlying corporate governance? Corporate governance is based on principles such as conducting the business with all integrity and fairness, being transparent with regard to all transactions, making all the necessary disclosures and decisions, complying with all the laws of the land, accountability and responsibility towards the stakeholders and commitment to conducting business in an ethical manner.

Why is it important? Fundamentally, there is a level of confidence that is associated with a company that is known to have good corporate governance. The presence of an active group of independent directors on the board contributes a great deal towards ensuring confidence in the market. Corporate governance is known to be one of the criteria that foreign institutional investors are increasingly depending on when deciding on which company to invest with regard to all transactions.

The advantages of corporate governance

Corporate governance refers to the ability of companies to manage themselves effectively. It is a collective system of leadership used by executives and all major leaders in the company, including important shareholders. It dictates how decisions are made and who holds the power in the company. A strong corporate governance system will be aware of the company’s current progress and will have the ability to make many changes in corporate structure as needed.

Enhanced performance. Corporate governance helps a company improve overall performance. Without corporate governance, a company tends to be weak and sluggish. Only a group of leaders working together can successfully foresee market changes and prepare the company to meet them ahead of time.

Access to capital. The better corporate governance a company has, the more easily it can access outside capital that the business can use to fund its projects. Since corporate governance includes major shareholders, it connects investors with the business itself, and these investors use their resources and contacts to support the company monetarily. Due to these close connections, capital also tends to be less expensive to finance with a strong corporate governance system.

Better standards. Corporate governance makes many decisions about business operations, but one of the most important decisions involves corporate standards. Standards affect the quality of products and the goals that the business has in technology, customer service, and marketing. The combined efforts of the business leaders allows the company to accurately judge competition and create standards that add value to the business’s products or services.

Better talent utilization. Without a corporate governance, business leaders tend to flounder. The lack of clear organizational structure at the top of the company makes it difficult for people to move up the ladder or to aim for a particular position. With a strong corporate governance structure, however, people can find positions that utilize their talents more effectively, and the board of directors and top leaders of the business are always looking to add more talented people to their numbers.

Seven characteristics of good corporate governance

In 1992, the King Committee of Corporate Governance was formed in South Africa with the intent of laying down recommendations for highest standards in corporate governance with a South African perspective. The Committee published its first report in 1994 which established recommended standards for the board of directors of certain listed companies. In 2002, the second King’s report was published which updated the Code of Corporate Practices and Conduct. The second King’s report also listed seven characteristics of good corporate governance.

Discipline. Discipline in corporate governance means that the senior management should be aware of and committed to adhere to behavior that is universally recognized as correct and proper.

Transparency. Transparency is the measure of how easy it is for outsiders to find out and analyze a company’s financial and non-financial fundamentals. Companies should make this information available in timely and accurate press releases to give outsiders a true picture of what is happening within the company.

Independence. For good corporate governance, it is important that all decisions are made objectively with the best interest of the enterprise in mind and without any undue influence from large shareholders or an overbearing chief executive officer. This requires putting in place mechanisms such as having a diversified board of directors and external auditors to avoid any potential conflict of interest.

Accountability. People who make decisions in a company must be held accountable for their decisions and mechanisms must exist to allow effective accountability. In public companies, investors hold individuals running the company accountable for their actions by carrying out routine inquiries to assess the actions of the board.

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Promoting good governance in development finance institutions

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Japanese investors adopt new stewardship code

Japanese Financial Service Agency (FSA) launched a Japanese version of “Stewardship Code” in February 2014, inviting institutional investors to sign up. Modeled on the British Stewardship Code adopted in 2010, these Principles for Responsible Institutional Investors were set out as a code of behavior for institutional investors who hold corporate stocks. In Japan’s stewardship code, “stewardship responsibility” is defined as the responsibility of institutional investors to enhance the medium- to long-term investment return for their clients and beneficiaries by improving the investee companies’ corporate value and promoting sustainable growth through constructive engagement or purposeful dialogue based on in-depth understanding of the companies and their business environment. The code defines seven principles considered to be helpful for institutional investors who behave as responsible institutional investors in fulfilling their stewardship responsibilities, with due regard both to clients/beneficiaries and to investee companies. To promote sustainable growth of the investee company and enhance the medium- and long-term investment return of clients and beneficiaries, institutional investors should:

- formulate and disclose a policy to fulfill their stewardship responsibilities
- formulate and disclose a policy on how they manage conflicts of interest
- monitor investee’s situations appropriately
- understand in common with the investee and work to solve problem through constructive engagement with the investee
- have a policy on voting and disclosure voting activity
- report periodically on how they fulfill their stewardship responsibilities, including their voting responsibilities, to their clients and beneficiaries
- have knowledge of the investee and their business environment, and consolidate skills and dialogue resources needed to make proper judgments in fulfilling their stewardship activities.


Ethics in business is extremely important; your reputation is all you have in life.”  
- Sir Freddie Laker

Decision making in business ethics

Facts. Decision making in business ethics usually requires companies to identify specific ethical standards, which often means different things to different people. As organizations continue to grow and expand, new individuals are hired who may not have the same ethical standards as individuals already working in the company. A difference in ethics often changes how individuals approach the decision-making process. Companies often use the organization’s mission statement to build a framework for helping individuals make ethical business decisions.

Types. There are five types of ethical standards: utilitarian, rights, fairness or justice, common good, and virtue. Utilitarian ethics is a standard that attempts to do the most good and limit the amount of harm for each individual. A rights approach protects and respects the moral rights of individuals impacted by decisions. The fair or just style seeks to create equality among all individuals while the common good method focuses on bettering society as a whole. The virtue tactic centers on the ideal virtues necessary for promoting individuals for the company.

Functions. Business ethics is a tool companies use to ensure managers, directors, or executive officers act responsibly in various business situations. Ethical decision making attempts to promote the company as a whole, rather than letting one individual profit from business decisions. Individuals who consistently make decisions based on their personal benefit may create legal liabilities for a company that can lead to bankruptcy.

Considerations. Creating an ethical business environment does not happen overnight. Companies may need to spend time and money training and promoting business ethics among managers and employees. Companies may also find implementing an ethical decision-making process may lead to negative feedback from managers or employees. Combating this negative feedback may be a difficult part of implementing business ethics.

Expert insight. Companies may use professional consultants, seminars, or other training methods to educate employees on decision making in business ethics. These outside sources may also be able to provide companies with an objective review of their current operations and offer advice on how to implement a strong ethical code in their business operations. While these professional resources may be expensive, it often helps companies develop an ethical business environment.


Responsibility. In a corporation, managerial responsibility means that the management be responsible for their behavior and have means for penalizing the mismanagement. It also means putting in place a system that puts the company on the right path when things go wrong.

Fairness. The company must be fair and balanced and take into the account the interest of all of the company’s stakeholders. In this sense, the rights of each of the groups of stakeholders must be recognized and respected.

Social responsibility. A well-managed company must also be ethical and be responsible with regard to environmental and human rights issues. As such, a socially responsible company would be non-exploitative and non-discriminatory.

http://www.ehow.com/info_8371727_seven-characteristics-good-corporate-governance.html

companies to invest in. It is also known to have a positive influence on the share price of the company. Having a clean image on the corporate governance front could also make it easier for companies to source capital at more reasonable costs. Unfortunately, corporate governance often becomes the centre of discussion only after the exposure of a large scam.

Why was it in the news recently? Corporate governance has most recently been debated after the corporate fraud by Satyam founder and chairman Ramalinga Raju. In fact, trouble started brewing at Satyam around December 16 (last year) when Satyam announced its decision to buy stakes in Maytas Properties and Infrastructure for $1.3 billion. The deal was soon called off owing to major discontentment on the part of shareholders and plummeting share-price. However, in what has been seen as one of the largest corporate frauds in India, Raju confessed that the profits in the Satyam books had been inflated and that the cash reserve with the company was minimal. Ironically, Satyam had received the Golden Peacock Global Award for Excellence in Corporate Governance in September 2008 but was stripped of it soon after Raju’s confession.


“Governance” is a quarterly publication of the Association of Development Financing Institutions in Asia and the Pacific (ADFIAP). It highlights ideas, best practices and trends in good corporate governance. Copyright, 2014, ADFIAP. Article contributions can be sent to robertj@adfiap.org