BUSINESS ETHICS
AND
CORPORATE GOVERNANCE

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D.D.C.E.
Education for All

UTKAL UNIVERSITY

Directorate of Distance & Continuing Education
Bhubaneswar

Reprint 2009

VIKAS® PUBLISHING HOUSE PVT LTD
A-22, Sector-4, Noida - 201301 (UP)
Phone: 0120-4078900 • Fax: 0120-4078999
Regd. Office: 576, Masjid Road, Jangpura, New Delhi 110 014
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ABOUT THE UNIVERSITY

Founded in 1943, Utkal University is the 17th University of the country and the first of Orissa. It is the result of the efforts of Pandit Nilakantha Dash, Maharaja Krushna Chandra Gajapati, Pandit Godavarish Mishra and many others who envisioned a progressive education system for modern Orissa.

The University started functioning on 27 November 1943, at Ravenshaw College, Cuttack. It originated as an affiliating and examining body but shifted to its present campus spread over 400 acres of land at Vanivihar in Bhubaneswar, in 1962.

A number of Postgraduate Departments and other centres were established in the University campus. There are presently more than two hundred general affiliated colleges under the University. It has eleven autonomous colleges under its jurisdiction, twenty-eight constituent postgraduate departments, 2 constituent law colleges and a Directorate of Distance & Continuing Education. It boasts of a centre for Population Studies, a School of Women's Studies, an Academic Staff College, a pre-school and a high school. The University also offers a number of self-financing courses.

NAAC accredited since 2003, with B++ status and a score little over 80%, Utkal University is recognized by the UGC. It is a member of the Indian Association of Universities and the Commonwealth Association of Universities.

DIRECTORATE OF DISTANCE & CONTINUING EDUCATION
UTKAL UNIVERSITY : VANI VIHAR
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From the Director's Desk

The Directorate of Distance & Continuing Education, originally established as the University Evening College way back in 1962 has travelled a long way in the last 52 years. **'EDUCATION FOR ALL'** is our motto. Increasingly the Open and Distance Learning institutions are aspiring to provide education for anyone, anytime and anywhere. DDCE, Utkal University has been constantly striving to rise up to the challenges of Open Distance Learning system. Nearly ninety thousand students have passed through the portals of this great temple of learning. We may not have numerous great tales of outstanding academic achievements but we have great tales of success in life, of recovering lost opportunities, tremendous satisfaction in life, turning points in career and those who feel that without us they would not be where they are today. There are also flashes when our students figure in best ten in their honours subjects. In 2014 we have as many as fifteen students within top ten of honours merit list of Education, Sanskrit, English and Public Administration, Accounting and Management Honours. Our students must be free from despair and negative attitude. They must be enthusiastic, full of energy and confident of their future. To meet the needs of quality enhancement and to address the quality concerns of our stake holders over the years, we are switching over to self instructional material printed courseware. Now we have entered into public private partnership to bring out quality SIM pattern courseware. Leading publishers have come forward to share their expertise with us. A number of reputed authors have now prepared the course ware. Self Instructional Material in printed book format continues to be the core learning material for distance learners. We are sure that students would go beyond the course ware provided by us. We are aware that most of you are working and have also family responsibility. Please remember that only a busy person has time for everything and a lazy person has none. We are sure you will be able to chalk out a well planned programme to study the courseware. By choosing to pursue a course in distance mode, you have made a commitment for self improvement and acquiring higher educational qualification. You should rise up to your commitment. Every student must go beyond the standard books and self instructional course material. You should read number of books and use ICT learning resources like the internet, television and radio programmes etc. As only limited number of classes will be held, a student should come to the personal contact programme well prepared. The PCP should be used for clarification of doubt and counseling. This can only happen if you read the course material before PCP. You can always mail your feedback on the course ware to us. It is very important that you discuss the contents of the course materials with other fellow learners.

We wish you happy reading.

(S.P. Pani)
DIRECTOR

UTKAL UNIVERSITY SYLLABI-BOOK MAPPING TABLE

Business Ethics and Corporate Governance

Syllabi	Mapping in Book
Unit-I Ethics and Business Ethics, Concepts Values and Ethics.	**Unit 1:** Introduction to Ethics **(Pages 3-25)**
Unit-II Ethical Corporate Behaviour, Its Development, Ethical Leadership.	**Unit 2:** Organizational Ethics **(Pages 27-40)**
Unit-III Ethical Decision-making, Ethical Dilemmas in Organization, Social Responsibility of Business and Corporate Governance.	**Unit 3:** Ethical Decisions **(Pages 41-111)**
Unit-IV Ethic in Functional Area, Marketing, Finance, Human Resource and Information Technology.	**Unit 4:** Ethical Issues in the Functional Area **(Pages 113-131)**
Unit-V Environmental Ethics, Corruption and Gender Issues—Gender Ethics, Sexual Harassment and Discrimination.	**Unit 5:** Environmental Ethics, Corruption and Gender Issues **(Pages 133-141)**

CONTENTS

INTRODUCTION

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For a very long time, there has been a real and a significant need for a good textbook on business ethics and corporate governance.

This textbook covers the issues related to corporate governance, business ethics, risk management and ethical decisions.

It tries to answer questions like,
- What is corporate governance?
- What is ethics and business ethics?
- How is risk managed in corporate governance?

This textbook is primarily intended for students of management in undergraduate, graduate and diploma courses in universities and colleges. However, we know that many such students are already managers anyway, who are undertaking part-time and distance education programmes of study. Hence, this book is written with the manager and the potential manager in mind.

When we look at the general scenario of Continuing Education in our country, we see that there is a tremendous potential and opportunity for providing flexible forms of learning, that complement the professional practices of managers and executives. For instance, when the learning has to be implanted by stand-alone resources (such as this textbook), one has to devise innovative means of imparting knowledge and skills. We have attempted to do precisely this: by presenting the learning material through a content exposition approach. In this approach, we begin with an introduction to the topic of the unit; then, we outline the learning objectives of the unit; and then we present the details of the contents in simple and easy-to-learn manner. At the end of each unit, we have a summary for quick recollection. Finally, we have carefully posed review questions to check your progress as you complete each unit of learning.

Obviously, how well a job we have done will be determined by you, the reader, as you go through the materials herein. We would be most grateful for critical comments and constructive suggestions to continually improve and refine the learning resources and educational value of this textbook.

How This Book Is Organized

This book is divided into five units:

Unit 1

This unit explains the ethical concepts and its different models. It also explains the different ethical theories and role of ethical actions in organizations. In addition, this unit defines the concept of social responsibility.

Unit 2

This unit discuss ethical behaviour as applicable to organizations. It also explains the significance of ethical leadership.

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Unit 3

This unit discuss the process of decision-making in organizations and the decision making models. It also discusses the ethical dilemmas faced by organizations and the social responsibility of business.

Unit 4

This unit deals with ethics in the areas of marketing, finance, human resource management, and information technology.

Unit 5

This unit gives a general overview of ethical issues in relation to the environment. It generally discusses the issues of corruption, gender ethics and sexual harassment.

UNIT 1 INTRODUCTION TO ETHICS

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Structure

1.0 INTRODUCTION

Ethics is the branch of philosophy that studies the values and behaviour of a person. Value study of a person is used to determine his positive and negative attitude towards life. Ethics studies concepts like good and evil, responsibility and right and wrong. Ethics can be distinguished in three categories: normative ethics, descriptive ethics and metaethics. Metaethics focuses on the issues of universal truths, ethical judgements and the meaning of ethical terms. Normative ethics can be used to regulate the right and wrong behaviour of individuals. Descriptive ethics, also called applied ethics, is used to consider controversial issues, such as abortion, animal rights, capital punishment and nuclear war.

1.1 UNIT OBJECTIVES

This unit teaches you about:

- Ethical concepts, models and values
- Self-development methods
- Types of ethical actions
- Benefits of business ethics

1.2 ETHICS AND BUSINESS ETHICS

1.2.1 Meaning of Ethics

The term 'ethics' defines the standards that bear on right and wrong issues of society. Business ethics is thus a set of professional standards, which emphasize principles of honesty and duty to the business and the general public. The other significant principles included in business ethics are:

- Fairness
- Integrity

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- Commitment to agreements
- Broad-mindedness
- Considerateness
- Importance given to human esteem and self-respect
- Responsible citizenship
- Attempt to excel
- Accountability

These principles, if strictly pursued, lead to a decent business environment and create healthy relationships in the organization. However, deviations from these principles can occur due to the following factors:

- Ignorance and indifference to issues
- Selfishness
- Imperfect reasoning

1.2.2 Concept of Business

Just like human beings function with limbs, corporations or companies function through their businesses. The term business can be broken as 'busy-ness' meaning thereby an activity that keeps an individual busy. In the economic sense, the creation of utility is called business while in the commercial sense, the activities concerned with the purchase and sale of goods and services are called business. A business includes that part of production, which is equally exchanged and results in mutual benefits to the parties who exchanged goods in the transaction.

Business Definitions

According to Peterson and Ploughman, 'Business may be defined as an activity in which different persons exchange something of value, whether goods or services for mutual gain or profit.'

According to James Stephenson, 'Business is the sum total of those processes which are engaged in the removal of hindrances of persons (trade), places (transport and insurance) and time (warehousing) in the exchange (banking) of commodities.'

According to F.C. Hooper, 'Business means the whole complex field of commerce and industry, the basic industries, processing and manufacturing industries and the network of ancillary services, distribution, banking, insurance, transport, and so on, which serve and interpenetrate the world of business as a whole.'

According to Section 2(13) of the Indian Income Tax Act, 1961, business means, 'any trade, commerce or manufacture or any adventure in the nature of trade, commerce or manufacture'.

Nature of Business

Business is a wide term. It includes all occupations in which people are busy in earning income either by production or purchase, sale and exchange of goods and

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services to satisfy the needs of people and to earn profit. The following points may be discussed to reveal the true nature of a business:

- **Economic activity**: Business is an essential economic activity. Profit motive is the key element that inspires a businessman to work efficiently.
- **Human activity**: Business is a human activity. In this sense, business is considered to be an economic activity of human beings only. A business is by the people and for the people.
- **Social process**: Business is a social process. All the individuals involved in a business, such as owners, customers and employees, are an integral part of society. Business has to fulfil its social responsibilities.
- **System**: A system is a combination of things or parts forming a unitary whole. It is an established arrangement of components for the attainment of objectives. Similarly, business is a system consisting of various subsystems that are operated in a balanced and coordinated way.

Types of Business Activities

All human activities concerned with earning money are included under the term business. Cultivation by a farmer, teaching by a teacher and treatment taken by a patient from a doctor are also treated as business activities.

There are different types of business activities, which may be classified as follows:

- **Industry**: An industry includes the activities connected with the production and processing of goods. Manufacturing enterprises are engaged in the production of goods. These kinds of industries can be classified as follows:
    - **Analytical enterprises**: An oil refinery that separates crude oil into petroleum, kerosene and diesel oil is an analytical concern.
    - **Synthetic enterprises**: An enterprise which combines several materials to produce one product is a synthetic enterprise. All soap mills and cement factories are synthetic enterprises.
    - **Assembling enterprises**: All those plants engaged in the production of products, such as radios, scooters and television sets are assembling enterprises. A few enterprises involved in mining are involved in mineral resource production, for example, iron ore, coal, gold and silver.
- **Commerce**: It is the total of all those activities that are engaged in the removal of hindrances of persons or trade, places or transportation, risk of loss or insurance and time, such as warehousing, banking and financing of commodities. Commerce can be divided into two categories: trade and aid to trade. Trade can be further divided into two categories, which are as follows:
    - **Internal**: This includes the trade that is done with the country, such as wholesale and retail trade.
    - **External**: This includes the trade that is done with various countries, such as export and import.

  Aid to trade can be divided into transport, banking and insurance.

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Figure 1.1 shows the types of business activities.

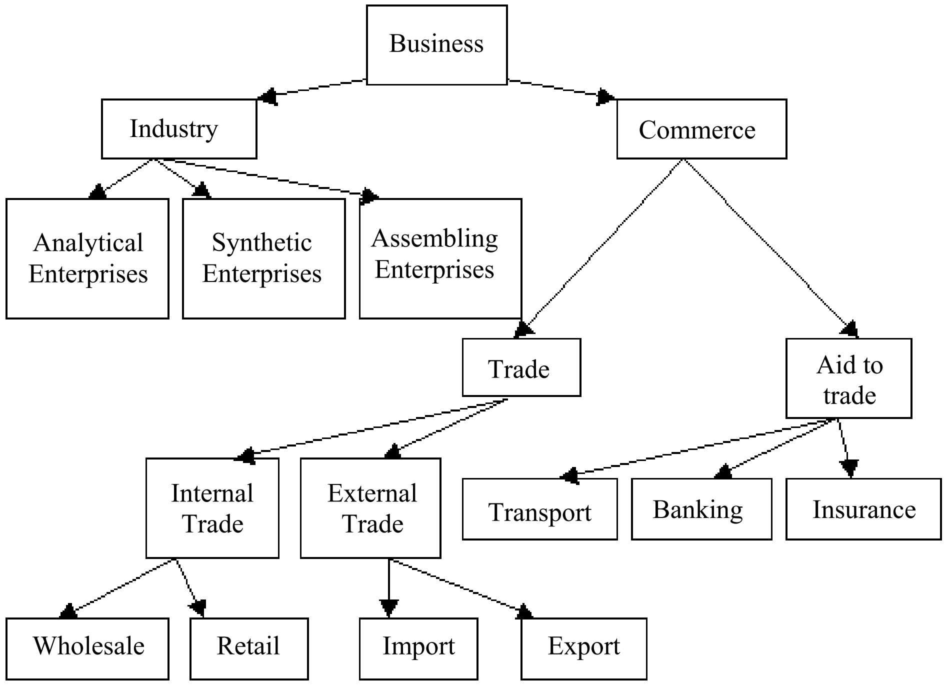

Figure 1.1: *Types of Business Activities*

Characteristics of Business

Business means the creation of utilities. There are many features of business activities and, thus, the business. The essential characteristics of business may be summarized as follows:

- **Exchange or sale**: A business includes the sale, purchase and exchange of goods and services.
- **Creation of utilities**: A business creates transfers and utilities of goods by making them available in proper form at the appropriate time and place.
- **Social institution**: A business deals with the people of society. All the persons engaged in the business, such as owners, customers, employees and other professionals, belong to the society. A business has to fulfil its social responsibilities towards each part of the community and has to follow the business ethics as well.
- **Profit motive**: Business activities are carried out to make profit. A non-profitable business cannot continue to exist for long. Profits are essential for growth of a business.
- **Risk and uncertainty**: There are two types of risks in a business. The first type of risk is floods and thefts. The second type of risk is loss due to fall in demand and labour trouble.

  Uncertainty arises because of unpredictability of profit in a business. Profit is such an element which cannot be predicted in advance.
- **Customer satisfaction**: A business always tries to satisfy its customer with better quality and reasonable prices.

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Business Goals

The term 'goals' denote what an organization expects to achieve in the future. A goal describes clearly the activities and tasks to be completed by an individual and a department or an organization. A business has a number of goals, which describe a desired future state for which efforts are directed. The goals are like a measure to evaluate the success of the business. It helps the management to keep the organization and the individuals working for it, away from distractive activities which come in the way of the success of an organization.

The characteristics of business goals are as follows:

- Business goals are derived from mission statements.
- Business goals are task oriented and, therefore, they must state what is to be achieved by an organization.
- Business goals are short term in nature.
- Business goals are challenging as they challenge the individuals who are responsible for its attainment.
- Business goals must specify the conditions that are necessary for the attainment of organizational goals.

Objectives of Business

Objectives are needed in every field where performance and results affect the survival and prosperity of a business. Success in a business cannot be achieved without the proper selection of objectives. The structure, direction and management of a business closely depend upon its objectives. Some of the important objectives are as follows:

- **Economic objectives**: Profit earning is the most important objective of a business. Profits must be earned by a business to provide for its own survival, coverage of risks, growth and expansion. It is a necessary motivating force and it is in terms of profits that the efficiency of a business is measured. All business activities are performed to achieve the following economic objectives:
    - **Incentive**: Profit is the biggest incentive for work. It is the driving force behind the business enterprise. It encourages a man to work to the best of his ability and capacity.
    - **Survival**: Profit is essential for the survival of a business. In the absence of profits, an organization will not be able to survive. It also helps in replacing obsolete machinery and equipment and, thus, ensures the continuity of a business.
    - **Growth**: Stagnation is the biggest setback for any industry. The prosperity and continuity of an industry largely depends upon its growth and expansion.
    - **Measurement of efficiency**: Profits measure the performance of the business. It is the accepted yardstick for the evaluation of the efficiency of the business.
    - **Prestige**: An unsuccessful business concern carries no good will. Higher profits not only provide economic power and status to the

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businessman but also improve the creditworthiness and bargaining strength of the business.

- **Social objectives**: The purpose of a business is not only to earn profits but also to discharge responsibilities towards society as well as employees. These objectives are as follows:
    - **Service to society**: A business must serve the society by considering the following factors:
        - **Better product**: Customer satisfaction is the backbone of a business. Therefore, a business must ensure a supply of better quality of goods and services to its customers.
        - **More employment**: A business provides a large number of employment opportunities to the members of the society. This is a very important service especially in developing countries like India where the pressure of population is high and thus unemployment prevails.
        - **Better environment**: No business can survive for long if it is harmful to the society. It must not cause any kind of air, water or noise pollution. All effort must be made to reduce the adverse effects of business on the quality of life. Men, animals and birds must also be protected from industrial pollution of the environment.
        - **Better living standard**: Good employment opportunities and good quality of products improve the living standard of the people.
    - **Service to employees**: A business must serve its employees by considering the following features:
        - **Fair wages**: Social justice requires that employees get fair remuneration for their work. Apart from the wages, if their employers acknowledge their contribution, the employees would be satisfied and would work more sincerely.
        - **Growth and promotion**: The work of the employees must be acknowledged and they should be given adequate training to improve themselves so that they will be ready to accept better positions in an organization, if offered.
        - **Partnership in the prosperity of business**: Employees should not be considered servants in an organization. Their contribution must be given due recognition. They must be allowed to share in the prosperity of the business either by sharing of profits or capital.
- **Human objectives**: The production process consists not only of materials, machines and land, but also the workers working for the organization. Different human objectives can be listed as below:
    - Fair wages, bonus, dearness allowance, provident fund, medical facilities and educational and other facilities to employees
    - Workers' participation in management
    - Encouragement of creativity, initiative and provision of growth opportunities for employees

- o Job satisfaction and other provisions to raise the morale of workers
- o Congenial working conditions
- o Security of employment for workers
- o Profit sharing schemes for the workforce

- **National objectives**: Apart from the other objectives, there are some national objectives as well which are as follows:
  - o Ensuring social justice
  - o Development of skilled personnel
  - o Development of small entrepreneurs
  - o Export development
  - o To abide by laws passed by local, state and central governments

Role of Objectives

Business objectives play a very significant role in strategic management. They help the management in the following ways:

- Objectives are the base of strategic decision-making. They help in strategic decision-making by directing the attention of strategists to the areas where decision-making is required by them and also by coordinating individuals' behaviour towards strategic decision-making.
- Objectives help in providing standards with the help of which both the individual as well as the overall performance of an organization can be judged.
- Objectives also define the relationship of an organization with its environment. This helps the organization to take into consideration what has to be achieved for its employees, customers and the organization itself.
- Objectives also help define the vision and mission statements of an organization.

1.2.3 Responsibilities of a Business towards Various Interest Groups

Interest groups consist of the various persons connected with a business, such as consumers, shareholders and the community. The responsibilities of a business towards various interest groups are as follows:

- **Responsibilities towards consumers**: A consumer is a person who determines what goods shall be produced and whether they should be sold in the market or not. Consumers not only determine the income of the business but also affect the success and survival of the business. Therefore, a business has some basic responsibilities towards the consumers and these are as follows:
  - o To produce those goods that meet the needs of consumers of different tastes, classes and purchasing power
  - o To establish the lowest possible price with efficiency and reasonable profit to the business
  - o To ensure fair distribution of products among all sections of the consumers

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  - o To make the products more satisfactory to consumers through the study of consumer needs
  - o To handle the complaints of consumers more carefully and to analyse them properly
  - o To answer consumers' enquiries related to the company, its products and services

- **Responsibilities towards shareholders**: The basic responsibility of a business is to ensure the safety of investment and higher rate of return on the investment. Owners of a business may be proprietors, partners or shareholders. The interest of shareholders lies in participating in the management and getting regular dividends at appropriate rates. It is, therefore, the responsibility of the management to improve communication between the company and its shareholders. This can be done by providing maximum information to the shareholders through newsletters, annual reports or by holding the annual general meeting of the company at an appropriate time and place so that the maximum number of members can come and participate in the discussions.
- **Responsibilities towards community**: The management has the responsibility of informing the community about the organizational policies, activities and contribution towards the betterment of society. The various other responsibilities towards the community are as follows:
  - o Financial help to the municipal and district boards for the improvement of housing conditions
  - o To help the community by aiding hospitals, schools, colleges, religious institutions, and so on
  - o To organize community forums and group discussions to promote better understanding of national and local affairs
  - o To encourage sports and provide recreational facilities

Business Ethics

Business ethics has different meanings for different people, but generally it is to decide what is right or wrong in the business. According to Wallace and Pekel, 'attention to business ethics is necessary during times of fundamental change as the moral values that were not taken seriously are strongly questioned at that time'. Business ethics enables the leaders and employees to act at the time of crises and confusion in the business. Therefore, business ethics helps to deal with business ethical issues that are vague.

1.3 ETHICAL CONCEPTS

Ethics is the branch of philosophy that is used to evaluate human actions. Some basic ethical concepts in business are as follows:

- **Ethical subjectivism**: This concept emphasizes that the ethical choice of the individual decides the rightness or wrongness of his behaviour.
- **Ethical relativism**: According to this concept, no principle is universally applicable and so it would be inaccurate to measure the behaviour of one society with another's principles or standards. Relativism overlooks the

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fact that there may be enough evidence to believe that an ethical practice is based on false belief, illogical reasoning, and so on.

- **Consequentialism**: Consequentialism is based on two ideas: the concept of value and the maximization of value. If, for example, honesty is considered a value, an act is considered ethical only if it maximizes this value. An act, which does not maximize the said value, is not ethically permissible.
- **Deontological ethics**: This concept stresses that ethical values can be developed from the concepts of reason as all rational individuals possess the ability to reason. We may, for example, end up causing pain unknowingly while trying to create happiness. Therefore, the ethical value of an action cannot be determined by its consequences. Instead, it is in the motive that lies behind the particular action.
- **Ethics of virtue**: This concept emphasizes those traits that give the individual a sense of satisfaction from ethical point of view. Virtuous acts like courage, honesty, tolerance and generosity are done as a way of living and not by chance.
- **Whistle blowing**: Whistle blowing refers to the attempt of an employee to disclose what he or she believes to be illegal behaviour in or by the organization. From one point of view, this seems to deceive the principle of honesty in business ethics, as it is taken for granted that the employees of an organization need to be loyal to its workings. However, when loyalty to one's organization in particular is perceived to be harming one's general loyalty to mankind, the act of whistle blowing is justified. Failure on the part of the management of the organization to fulfil its social obligations calls for whistle blowing. It is the responsibility of the whistle blower to be careful about revealing the organization's secrets and to consider the harm it may cause to his colleagues and shareholders. The steps that should be taken into consideration by the whistle blower are:
    - Ascertain the gravity of the situation before whistle blowing
    - Scrutinize the purpose
    - Authenticate and keep a record of the concerned information
    - Determine the type of offence and to whom it should be reported
    - Assert your claim in a proper way
    - Stick to the facts
    - Determine if the whistle blowing need be external or internal
    - Decide if the whistle blowing should be anonymous or otherwise
    - Make sure to follow proper rules in reporting the offence
    - Consult a lawyer (if required)
    - Anticipate and document vengeance
- **Ethical dilemmas in business**: An organization's ethical problems indicate a conflict between its economic and social performance. This results in a dilemma for managers. Since people handle business, it is a crucial requirement to check and ascertain ethical behaviour at a personal level. This will confirm ethically correct responses from the organization to the mutual actions of individuals.

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1.3.1 Ethical Models

Ethical models can be used to define ethical situations and manage ethical dilemmas that may occur in the organizations. The Golden Rule Model and The Right-driven or Kantian model are two operational models that have emerged from the work of philosopher Immanuel Kant .

The Golden Rule Model

This model—originated from the New Testament—specifies people should treat others in the same manner that they themselves would like to be treated. It is a fundamental principle found in every culture and religion and it is the most important basis for the modern concept of human rights. It is also called the ethics of reciprocity as it stimulates an individual to put oneself in the other person's shoes and then evaluate how one would wish to be treated in that particular situation. This proves that this rule is absurd without identifying the receiver and the situation. The ethics of reciprocity should not be confused with revenge or penalizing justice. The ethics also mentions that one has the freedom to do anything as long as those activities do not harm anyone. If this golden rule is applied to every anomaly, then many unethical consequences may result in causing harm to others and perfectionists may charge others with critical analysis, which may lead to harassments. Different people have different ideologies, beliefs and may belong to different cultural heritages. This difference is the reason behind the difference people's behaviour towards various situations.

The Kantian Model

This model is based on the hypothesis that everybody has some fundamental rights in this ethical universe. So any action is ethically correct if it reduces the stakeholders'collective violation of rights. This model willingly provides assistance in the internal audit review and helps in managerial decision-making. Kant did not believe that any outcome was good from its origin. According to him good is not always intrinsic. He did not believe in 'good' character traits like ingenuity, intelligence and courage. In fact, he used the term 'good' to describe 'goodwill', by which he meant the resolve to perform the act purely in accordance with one's duty.

If the actions are predetermined then they cannot be described as free and moral. He believed that to act morally, freedom is required. According to Kant there are two concepts of duty. According to one concept, duty is just following orders imposed by others. The other concept is that duty is internal and can be imposed on oneself. He considered that inclinations constitute motivation whereas others believed that it was the physical world that acted as motivation. But Kant believed that the sources of the physical world might be unreliable, passive and phenomenal. Sometimes, man's mind is over-clouded by sorrows due to his lack of sympathy from others but he still has the power to help those in distress. He no longer needs any support as he is sufficiently occupied with his own inclinations, making him indifferent to the sufferings of others. He becomes adaptive to his sufferings with the help of the patience and endurance he has developed in due course of time. This begins to show his worth of character and temperament.

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Most of us live by rules most of the time. Some of them are called categorical imperatives that are unconditional commands which bind everyone at all times. There are two types of imperatives: hypothetical imperative, which is to say that if one wants to achieve success then he should work in a free way and not bind himself to his inclinations; and categorical imperative, for example, the imperative to always tell the truth as it is unconditional and can be applied at all times.

Kant also introduced maxims, which are subjective rules that guide actions and help an individual to act according to the relevant description. There is sufficient generality in description. All actions have maxims like:

- Never lie to your colleagues.
- Never act in a manner that would make your family or organization ashamed of you.
- Always work hard to be the best performer.
- Its acceptable to cheat if the pattern demands it.

1.3.2 Virtue Ethics—An Alternative Model of Ethics

The traditional ethical models of utilitarianism and Kantian ethics ignore the character of the agent who delivers the action and focuses primarily on the action as the main theme of ethics. Utilitarianism tells us that actions are right according to the happiness that emerges as the outcome, while Kantian ethics tells us to 'act only according to that maxim whereby you can at the same time will that it should become a universal law'. The morality of human beings and their actions are evaluated by the alternative approach to ethics. The fact that actions form the basic subject matter of ethics has been criticized by several ethicists. This assumption highly debated the fact that ethics should also pay attention to the kind of person an agent ought to be and not just focus on the action of the agent. This helps to carefully judge a person's moral character which includes whether his moral character displays vice or virtue. According to ethicists, an adequate approach to ethics takes virtue and vice as the fundamental beginning for ethical point of view in contrast to the action-based ethics. However, it does not believe that ethics of virtue vary majorly from the action-based ethics. It is said that moral virtue is obtained and is appreciated as part of a good human being who is morally high and this is revealed in the habitual behaviour of the person. A person is said to possess moral virtue when he is inclined to act normally in the way that are the characteristics of a morally sound person. For instance, honesty is regarded as an attribute of a person who is morally good.

When a person believes that telling the truth is right and he feels good when he speaks the truth he is said to be honest by virtue. He habitually speaks the truth and does so because when he lies he is uncomfortable and therefore, tells the truth out of respect for truth. If a person spoke truthfully occasionally or spoke the truth with immoral desires, or for wrong motives, in that case he is not honest. A person cannot be called honest if he lies frequently, or if his motive for telling the truth was to get people to like him or out of fear. Honest as a moral virtue has to

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be acquired and is not just a normal characteristic like beauty or intelligence. Possessing a moral virtue is worthy of praise because it is like an accomplishment since it needs effort. The question that arises from this standpoint of ethics is: What are the characteristics that make a person morally good? Which traits are termed as moral virtues? There are several views based on these. The most noteworthy theory of virtue was by Aristotle who was of the opinion that moral virtue is a like a habit that allows a person to perform an action in harmony with the definite goal of human beings. Aristotle distinguished human beings from all other living beings by their capacity to reason and therefore, the main purpose of human beings is to use reason in all their actions and behaviours. Therefore, it can be said that moral virtues are habits that allows a human being to live with reason. Aristotle was of the opinion that a human being lives his life in accordance to reason. Moral virtues makes a human being aware and he selects the reasonable ground in his actions, emotions and desires by going too far and still not going far enough. Moral virtue draws a line between two vices, one of lack and the other of surplus, and its purpose is to hit the mean in reference to desires, actions and feelings. Consider this example, in case of the emotion fear, courage is the virtue in response to fear while cowardliness is a vice in response to fear and recklessness. In case of desire for food, restraint is the virtue which restrains you from indulging in excess while gluttony is the vice that leads to indulging in excess and austerity is the vice of unfairly indulging in too less. Justice is the virtue that gives people what they are worthy of whereas injustice either gives them less or more than they are worthy of. Virtues, therefore, deal with one's aspirations, actions and emotions in a way that takes the sensible middle path and keep away from irrational extremes, whereas vices leads to the extremes of either surplus or too less. Aristotle argued that the virtue that allows a person to identify what is reasonable in a situation is prudence. A Christian philosopher of the middle ages, St Thomas Aquinas, was of the opinion that a person's purpose is not just to use reason, but also the union with God. Thus, Aquinas added the theological or Christian virtues of hope, charity and faith—the virtues that permit a person to unite with God—to Aristotle's list of moral virtues. So far one significant facet of virtue theory has been ignored: How does it help a person to decide what he should do? Can a virtue ethic give person guidance about how he should live his life and how he should behave? There is an analysis that criticizes virtue theory by saying that it is unsuccessful in providing guidance on how one should act. In a situation when a person is in a dilemma or about to commit an act which he is unable to decide if his action is right or wrong, it is likely he will ask a friend for a solution, it does not help to be told what kind of character one should have. In such circumstances, one requires advice on what type of actions are suitable in a given condition, and the virtue theory seems incapable of giving such advices.

CHECK YOUR PROGRESS

1. Define the term ethics.
2. List two different types of models of ethics.
3. What are the different ethical business concepts?
4. Name an alternative model of ethics.
5. What is the golden rule model?

1.4 ETHICAL VALUES

Ethical values and actions are an integral part of ethical societies. Ethical actions in the ethical society refer to the initiatives taken by the people to show their commitment towards building a better life for them and for their children. Ethical actions are also termed as the categorical imperative actions. The whole world is created by action and is meant for action. The future life depends on the actions performed by the people. Ethical actions are the activities performed by the social, national or personal group. The people in these groups perform the activities in a spirit of service and commitment. The dimensions of ethical actions can be divided into two major categories. These categories are:

- **Community service**: Community service aims at helping the organizations and the people in the community. The organizations in the Baltimore area providing food to AIDS victims and their families come under this category.
- **Social issues support**: Social issues support aims at giving emotional and physical support to organizations and the people in the society. Social issues support can come in different forms. These forms are:
    - Emotional support
    - Informational support
    - Instrumental support
    - Personal feedback
    - Sharing view points

1.4.1 Types of Ethical Actions

Ethical actions can be of two types. These types are:

- Destructive actions
- Constructive actions

Destructive Actions

Destructive actions are those that can harm the people performing the actions as well as others. It is very difficult for people to find out which actions are harmful. Some actions can cause damage in one situation and the same actions can be useful in some other situation. Buddhist ethics point out that the motivation and frames of mind are the two concepts that can be useful to determine destructive actions. A destructive action must be motivated by passion, anger and naivety about its effects. Buddhist ethics determined that most of the mental, physical and verbal actions could be destructive. The ten destructive actions determined by Buddhist ethics are:

- Taking the life of others
- Taking something from others that has not been given to them
- Lying
- Talking and speaking insensitively
- Using cruel language
- Using language consisting of idle words
- Thinking thoughts of meanness
- Thinking jealous thoughts
- Distorted and aggressive thinking
- Behaving like a moderator

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Constructive Actions

Constructive actions are also considered as desire-prompted duties. Constructive actions are always done by people who consider it their responsibility or duty to perform these actions. These actions can be performed either daily or on some special time. These actions always provide a result that is purposeful and self-determined. Constructive actions can be of three different types. These types are:

- **Obligatory actions**: These actions can be performed by any type of person in the society. These actions do not affect any special category of people. Every man, society and the universe would be affected by these actions.
- **Prohibited actions**: Prohibited actions do not prove to be of worth for the people. The non-performance of prohibited actions is also obligatory.
- **Optional action**: Optional actions are also called hypothetical imperative actions. These actions prove to be beneficial to human beings and are also performed by the people to secure their personal benefits.

Therefore, ethical actions are responsible for performing the obligatory and optional actions successfully and avoiding the prohibited actions.

Characteristics of Ethical Actions

The different characteristics of ethical actions are:

- Ethical actions are not only activities to serve others but also the inner temperament of the mind.
- Ethical actions give importance to helping others.
- Ethical actions are not the instrumental value but the intrinsic value.
- Ethical actions are performed for prosperity, success and sound decisions.
- Ethical actions are used to avoid prohibited constructive actions and to promote obligatory and optional actions.
- Ethical actions are performed as duties or responsibilities of individuals.

Karma Yoga

Karma yoga is also referred to as the Buddhi yoga or the discipline of actions. Karma yoga is one of the four pillars of yoga. Karma yoga gives importance to perform the ethical actions and not care for the results or reward. It states that the only way to spend life successfully is to perform ethical actions regularly. According to karma yoga, people performing ethical actions can achieve Moksha and blessings of God. Ethical actions are a way to perform duties or responsibilities in an unselfish manner. Individuals performing ethical actions without care for the fruit would be detached from this world. Only these persons can understand the truth of life. Indian Hindu culture is derived from this philosophy.

People with belief in the karma yoga are able to face any type of situation in life and can also explain the results of their ethical actions to others. The person

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performing ethical actions by keeping the karma yoga principles in mind spends a truly moral and more satisfied life. The principles of karma satisfy the logical as well as the moral awareness of people. People following the principles of karma yoga understand that:

- They have to perform only ethical actions.
- They should not be concerned with the results of their ethical actions.
- They should not perform ethical actions to get a predefined result.
- These principles do not force people to sit idle.

Morality

People should be self-disciplined in order to carry out ethical actions successfully. Morality refers to the concept of human action which pertains to matters of right and wrong. Individuals who oppose with determination inducement towards the wrong spend a good moral life.

Ethical actions should be performed as a community standard rather than as an individual responsibility. Individuals in a society can perform three types of ethical actions. These actions are:

- **Morality**: Morality actions are performed to secure the future of others.
- **Religion**: Religion is the collection of ethical actions that can affect a group or society.
- **Civil law**: Civil law actions are a collection of ethical actions that can be used to change or control the behaviour of an individual in society.

Therefore, morality can be defined as the collection of concepts and attitude that can be used by a culture or a group in society to control or change the behaviour of an individual. Different societies or cultures have their different opinions on morality. Morality can be applied to the generality or the part of the fields in which the personal opinions of the individual have some relation or reference to other individuals. These individuals may belong to some other community too. Therefore, morality can exist in isolation or in a generic society.

There exist different types of groups or societies having different views on behaviour. Some groups put heavy restrictions on behaviour and some groups allow the individuals to be self-determined. Morality can also be defined as the personal ethical behaviour that an individual creates for himself.

The terms 'morality' and 'ethics' have a strong relationship with each other. Morality refers to moral character or standards. Morality is used to analyse the behaviour of the individual and the standards of conduct. Ethics is used to refer to the formal study of these standards. Morality can be considered as ethics in action.

Figure 1.2 shows the relationship between morals, values and ethics.

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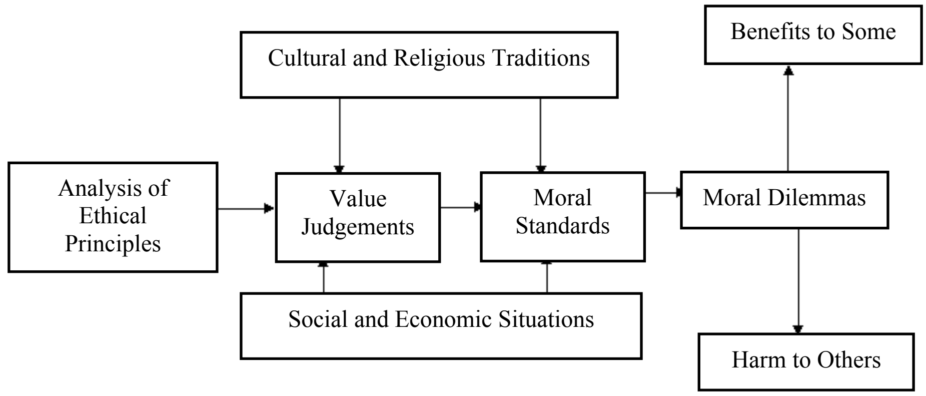

Figure 1.2: *Relationship between Morals, Values and Ethics*

The mind is responsible for the thoughts and feelings of individuals. The existence of individuals and their activities is only due to their mind. The feelings and opinions of persons depend on their mind. A person having a good mind has good feelings and a person having a disturbed mind has disturbed feelings.

Professor Gardner suggests five types of minds. The ethical mind is one of them. The others are disciplined mind, synthesizing mind, creating mind and respectful mind. The ethical mind of a person is affected by the nearby surroundings and culture. Ethical minds can be of two types. These are:

- **Subjective mind**: The subjective mind faces motivation from the different objects of the world. This type of human mind is also called the outer mind.
- **Objective mind**: This type of mind reacts to the encouragement received from the outside world. This type of human mind is also called the inner mind.

Figure 1.3 shows the two types of ethical minds.

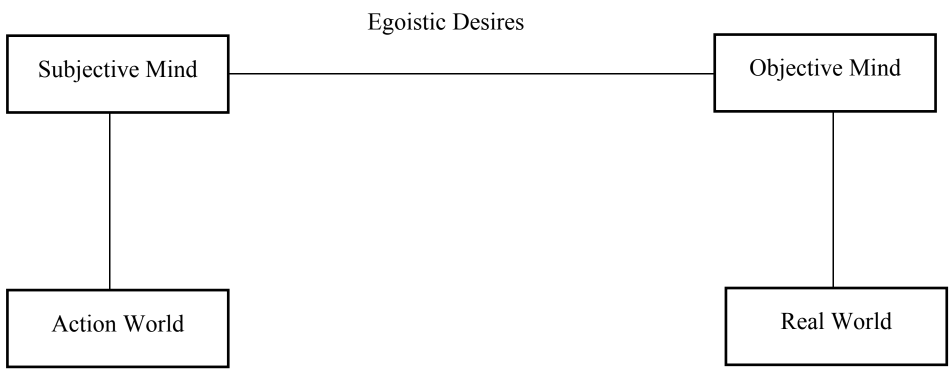

Figure 1.3: *Subjective and Objective Minds*

The objective mind of the human being is under the control of the subjective mind. The objective and subjective minds of human beings are separated by layers of egoistic desires. The confidence of an individual depends on the distance between these two minds. The greater the distance between these two minds, the more confused is the person. If the distance between the two minds is

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large, then the objective mind does not receive any message from the subjective mind. If the mind is in a state of confusion, then the mind of the individual becomes nervous, unsteady and confused. Thus, the person loses his morale. If the emotions of the person are separated from his mental power, then the objective mind would not be under the control of the subjective mind. This situation can make a man wild and come to some unintelligent conclusions.

Each person should try to decrease the distance between the subjective mind and the objective mind. This can only be accomplished by training the mind. Each person should be able to identify support that will maintain mental energy, intellectual vision and physical patience to spend the ethical action life.

Training of the mind can be accomplished by two methods. These methods are:

- **Art of disengagement**: Mental disengagement can only be developed by developing a mind that is free from abstracted and fractional feelings and is more concentrated. Every person should identify his role and keep the subjective and objective mind steady to fulfil his role. The mind of the person should be integrated so as to keep him aware of each situation. The integrated mind does not allow the individuals to cross the boundaries of his current role.
- **Self-denial**: Self-denial is an inner characteristic of a person, by which he does not let any extraneous thoughts enter his mind so as to achieve something. This is one of the methods to train the mind. Some examples of self-denial are the state of mind of a student before an examination, and the state of mind of a dancer before the performance.

1.4.2 Self-development

Self-development is the responsibility and duty of the individuals to learn and develop themselves. Individuals can use the process of assessment, reflection, and take necessary action to achieve self-development. Self-development is the only way for individuals to update their skills and knowledge in order to face the new problems that emerge in life. Self-development also determines one's future career direction. Some of the characteristics of self-development are:

- The person undergoing self-development does not depend on the support of the outside world. Such type of person becomes self-sufficient. Self-development in individuals makes them independent.
- Self-development brings in the feature of objectivity in individuals. Such a feature gives individuals an impersonal attitude.
- A self-developed person looks happy in life. His inner nature looks full of cheer and joy. He will not be depressed and miserable.
- A self-developed person becomes dynamic, active and brighter in life.
- A self-developed person is more lovable.

Self-development Methods

Individuals can use different methods for self-development. Some of the methods are:

- **Path of action**: The path of action is also called as karma yoga. Karma yoga is one of the four pillars of yoga. The path of action states that people should only perform their job and should not care for the fruits or

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results. This is also the Indian philosophy. Ethical actions are a way to perform one's duties or responsibilities in an unselfish manner.

- **Path of knowledge**: The path of knowledge means to move towards acquiring knowledge. The path of knowledge also eliminates the distance between the subjective mind and the objective mind. Thus, the path of knowledge makes a man confident and self-developed.
- **Path of discrimination**: The path of discrimination assists a person to identify his inner faults. The person has to transform the inner motives and mental attitudes to train the mind. The path of discrimination forces individuals to control the emotions of attachment, fear and anger.
- **Path of sacrifice of wealth**: The path of sacrifice of wealth refers to donations of wealth in charities without a consequence in mind. This feature makes people more positive towards life and helps individuals overcome greed.
- **Path of self-control**: Self-control is an internal characteristic of individuals. Self-control can be of five types. These are:
    - Non-injury
    - Truthfulness
    - Non-stealing
    - Celibacy
    - Non-acceptance of gifts
- **Path of mind-control**: The path of mind-control consists of concentration and meditation. Concentration refers to focusing on the object on which one is working. Devotion to God helps in achieving concentration. Meditation refers to the state of the body in which the person feels relaxed and the mind is more focused. Therefore, meditation helps in achieving concentration. The path of meditation is also called the path of yoga. Yoga is the only way to keep the mind calm and focused and hence to get concentration.

1.5 BUSINESS ETHICS

Business is described as an activity done by humans to produce or acquire wealth where he buys and sells goods. Business ethics and values are important for the successful development of a business organization. Ethics in business refer to a code of standard by which one can determine what is wrong and what is right for the business enterprise. Fairness, integrity, commitment to agreements, broad-mindedness, considerateness, importance given to human esteem and self-respect and many such principles determine business ethics.

Business ethics generally deals with what is right or wrong in the business. According to Wallace and Pekel, 'attention to business ethics is necessary during times of fundamental change as the moral values that were not taken seriously are strongly questioned at that time'. It is business ethics that enables the leaders and employees to act in times of crisis and confusion in the business. Business ethics is a method of dealing with unclear business problems.

1.5.1 Unethical Problems in a Business

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- **Managerial misbehaviour**: Managerial misbehaviour includes illegal and unethical practices involved in the management of an organization.
- **Moral mazes**: It is a part of business ethics which deals with the 'moral mazes of management'. It includes ethical problems, such as conflicts of interest, misconduct of contracts and agreements and the illegal use of resources. After the birth of the social responsibility movement in 1960, business ethics has become a management discipline. This movement helped solve various social problems, such as poverty, crime and illiteracy by using the finance of business class people.

To develop better relationships among people within an organization, the field of human resources emerged recently. As the complexity in the field of commerce has been increasing day by day, so has the need to simplify trade in an organization. The process of simplifying the commerce within an organization ensures better trading between the partners. With the growing need of simplifying trade, the discipline of business ethics emerged. Business ethics is managed by following the ethical code and the code of conduct as set by an organization.

1.5.2 Myths regarding Business Ethics

Business ethics maintains moral values and ensures that the behaviour of employees is aligned with these values. Still, there are certain myths regarding business ethics, which are as follows:

- Business ethics is a matter of belief than management.
- Organizations believes that their employees are ethical so they are not required to pay attention to business ethics. According to Wallace, ethical conflicts arise in the following situations:
  - When there exist significant value conflicts among differing interests of employees.
  - When other alternatives are equally acceptable.
  - When there are significant consequences on the 'stakeholders' of an organization.
  - According to Kirrane, people consider honesty and courtesy as the only business ethics. But when the complex ethical problems come into play, most people realize that it is difficult to apply ethical principles in real-life situations.
- Business ethics constitutes the principles propounded by philosophers and theologians. Many people are of the opinion that business ethics is a religion or a theoretical debate. In the day-to-day issues of the organization, business ethics has very little to contribute. However, ethics is a management discipline that requires a planned approach and several management programmes.
- Business ethics only states the obvious do-good situations. Several people are of the opinion that ethics represents the values that a person should naturally aspire to have and, therefore, establishing codes of ethics is unnecessary. However, importance should be given to the ethical values of an organization. For instance, it is understood that everybody should be honest. If the workers of an organization are not honest then the code of

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ethics of that organization should have honesty listed in it. Code of ethics changes with the change in the society and the needs of an organization.

- Business ethics is an opinion. Many people believe that stress and confusion may inspire good people to behave unethically. Ethics in an organization can be managed by helping each other to stay ethical and to work together through confusing and stressful ethical dilemmas.
- Business ethics is the new trend. Many people believe that business ethics is a recent phenomenon and has recently gained attention. However, it is an old phenomenon that has received importance now.
- Business ethics is unmanageable by an organization. Actually, ethics is not directly 'managed' by an organization, but the behaviour of the team leader has a strong moral influence on the employees. The objectives of an organization, such as maximizing profit and minimizing costs also have a strong impact on the ethics of an organization. Even the laws, regulations and rules have a good impact on the ethical values of the employees and hence minimize the harm to the business. But still, some believe that business ethics cannot be managed by an organization.
- Business ethics is a social responsibility. Many people believe that ethics is a social responsibility that does not deal with practical matters. Madsen and Shafritz define business ethics as an application of ethics to the corporate world. It helps in determining business dealing responsibilities and also identifies significant business and social issues.
- Business ethics is not needed if the organization has no legal problems. People are of the belief that persons who are unethical can function within the limits of law. For example, complaining constantly about others and withholding information from superiors. However, breaking the law often starts with unethical behaviour that has gone unnoticed.
- Business ethics has little practical significance in a business. Business ethics helps identify and prioritize the values to guide the behaviour of employees in an organization and establish associated policies and procedures for ensuring that a certain behaviour is followed.

1.5.3 Benefits of Business Ethics

The various benefits of managing ethics in a business are as follows:

- Business ethics helps in improving society by establishing government agencies, unions, laws and regulations in the society.
- Business ethics helps an organization maintain ethical values during times of crisis. Business ethics programmes guide leaders about the right or wrong ways of dealing with complex dilemmas and how they should act during that time.
- Business ethics helps employees behave according to the ethical values that are preferred by the top management of an organization. An organization discovers many differences between the values that reflect in the actions of the employees and the values preferred. Employees experience a relationship that is strong between the values of the organization and their values. Ethical values induce teamwork and increase the efficiency of the employees.

CHECK YOUR PROGRESS

6. What do you understand by self-development?
7. Mention two benefits of business ethics.

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- Ethics supports employee growth. When an employee pays attention to ethics, it induces confidence in the employee to deal with reality and face both good and bad circumstances. Bennett, in his article 'Unethical Behaviour, Stress Appear Linked', explained that the more an employee is emotionally healthy, the more ethical he is.
- Ethics have become legal instruments. These days, there are several lawsuits regarding personnel matters and the influence of the services of the organization on the investors and customers. Major ethical principles that are applied in the organization are the laws that are made by the government. A greater attention on ethical issues on the part of the government ensures high ethical procedures and policies in the workplace. An employee, for example, is subject to breach of contract on non-compliance of the terms and conditions of the contract.
- Business ethics helps to avoid criminal acts of 'omission' and it also helps in lowering the fines. Ethics helps in ascertaining the violation of ethical issues and helps in rectifying the violation that is committed by the organization. The guidelines set by an organization about ethical values helps to lower fines. An organization, for example, that has knowingly violated a contract is considered to have committed a criminal act and the organization is subject to penalty.
- Business ethics helps to identify and manage the values associated with quality management, strategic management and diversity management. For managing these values, ethical programmes record the values, develop policies and procedures and then provide training to the employees on these policies and procedures. These ethical programmes manage certain values of quality management, such as reliability, performance, measurement and feedback. Similarly, these programmes also manage various strategic values, such as reducing cost and increasing market share.
- Business ethics helps in building a strong and positive public image of an organization. Ethical values enable an organization to increase their goodwill in the market. Those organizations that value their customers have a positive influence in the market. Ethical values are the milestones that enable the establishing of a successful and socially responsible business.
- Business ethics strengthens organizational culture. Ethical values improve relationships between an organization and its customers. They strengthen the organization by ensuring consistency in the standard and quality of the product.
- Business ethics makes sure that the right activities are performed in an organization.

1.6 SUMMARY

Ethics is the branch of philosophy that is used to evaluate the attitude and behaviour of a person. Ethics is also used to analyse human actions. The Golden Rule and the Kantian model are the two basic models that can be used to define the ethical situations and manage ethical dilemmas that may occur in organizations.

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Ethical actions in the ethical society are used to represent the initiative taken by the people to show their commitment to their work. Ethical actions can be of two types: destructive and constructive. The ethical mind is also used to represent the thoughts and feelings of the individuals. Subjective and objective minds are two kinds of ethical minds.

Ethical management is a term used in organizations to handle different ethical dilemmas. Social responsibility of businesses involves the consideration of general public interest by businessmen while taking business decisions and actions.

1.7 ANSWERS TO 'CHECK YOUR PROGRESS'

1. (a) The term 'ethics' defines the standards that bear on right and wrong issues of society.

   (b) 'Ethics' is the branch of philosophy that is used to study the values and behaviour of a person.
2. Ethical models can be used to define ethical situations and manage ethical dilemmas that may occur in the organizations. Two operational models have emerged from the work of philosophers and theologians: The Golden Rule Model and The Right-driven or Kantian model, propounded by philosopher Immanuel Kant.
3. The basic ethical concepts in business are:
   - Ethical subjectivism
   - Ethical relativism
   - Consequentialism
   - Deontological ethics
   - Ethics of virtue
   - Whistle blowing
   - Ethical dilemmas in business
4. Virtue ethics is an alternative model of ethics which looks at moral issues and evaluates the morality of people's character and their actions.
5. The Golden Rule Model is derived from the New Testament and it states that one should treat other people in the same way that he or she would want to be treated. It is a fundamental principle found in every culture and religion and it is the most important basis for the modern concept of human rights. It is also called the ethics of reciprocity as it stimulates an individual to put oneself in the other person's shoes and then evaluate how one would wish to be treated in that particular situation.
6. Self-development is the responsibility and duty of the individuals to learn and develop themselves. Individuals can use the process of assessment, reflection, and take necessary action to achieve self-development. Self-development is the only way for individuals to update their skills and knowledge in order to face the new problems that emerge in life. Self-development also determines one's future career direction.

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7. The benefits of business ethics are:
   - Business ethics helps in improving society by establishing government agencies, unions, laws and regulations in society.
   - Business ethics helps an organization maintain ethical values during times of crisis. Business ethics programmes guide leaders about the right or wrong ways of dealing with complex dilemmas and how they should act during that time.

1.8 EXERCISES AND QUESTIONS

1. What are the types of business activities?
2. Discuss the different ethics models.
3. What are the characteristics of ethical actions?
4. What do you understand by business ethics? What are its benefits?

1.9 FURTHER READING

Modh, Satish, *Ethical Management: Text and Cases in Business Ethics and Corporate Governance.* New Delhi: Macmillan Publishers India Ltd, 2005.

Mathur, U.C., *Corporate Governance and Business Ethics: Text and Cases.* New Delhi: Macmillan Publishers India Ltd, 2005.

UNIT 2 ORGANIZATIONAL ETHICS

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Structure

2.0 INTRODUCTION

To understand the term 'organizational ethics', one has to first try and understand the two terms 'organization' and 'ethics'. An organization is a collection of individuals with a common mission while 'ethics' may be described as an attempt or endeavour by individuals, to understand what is 'right' or 'wrong'. Ethics is concerned with the critical analysis of situations.

Organizational design and follow a set of core principle or concepts in that attempt to develop ethical corporate behaviour.

2.1 UNIT OBJECTIVES

This unit teaches you about:

- The collective scope of organizational ethics
- Corporate code of ethics
- Framing a code of conduct
- Managing ethics in an organization
- Roles and responsibilities in ethics management

2.2 ETHICAL CORPORATE BEHAVIOUR

Organizational ethics is used to consider the issues of morality and rationality in organizations. Organizational ethics is completely different from management ethics. Management ethics focuses on the ethical quality of the decisions and actions taken by managers of an organization. Thus, management ethics deals with the individuals in the organization and organizational ethics deals with all the activities of an organization. Therefore, organizational ethics is collective in scope.

Organizational ethical issues can be handled at three levels. These levels are:

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- Corporate mission
- Constituency relations
- Policies and practices

Corporate mission refers to the objectives of an organization that are used to define its ethical responsibilities. Corporate mission also reflects the ambitions and expectations of the employees. Employees should be integrated in a good manner to achieve the corporate mission.

Constituency relations define the responsibilities of the elements of an organization. The elements of an organization may be employees, customers, suppliers, shareholders and the general public. These responsibilities must be handled properly to manage the ethical conduct of business.

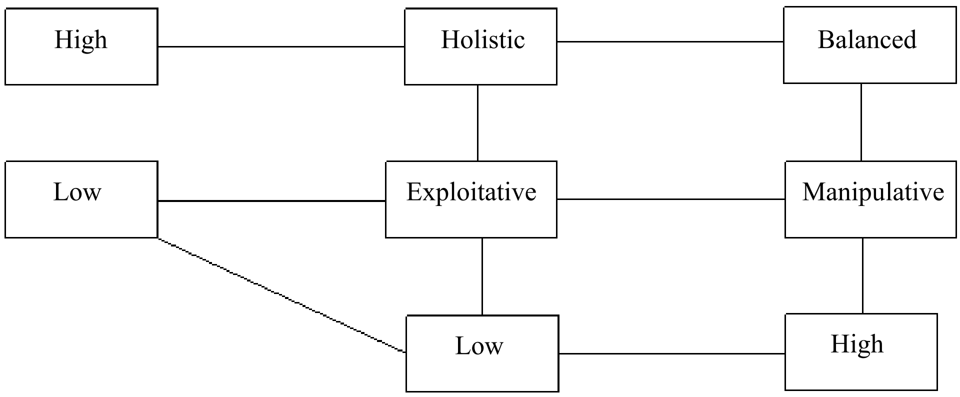
Organizational ethics can also be used to evaluate the policies and practices of the organizations. Public commitment to ethical principles can give way to business and administrative practices.

Organizational ethics also depends on the type of the organization. Organizations can be classified by considering their economic and ethical concerns. Organizations can be classified into four types. These are:

- **Exploitative**: Organizations with low economic and ethical concerns are called exploitative organizations. These organizations utilize child labour and use rivers for dumping wastes to maximize their profits.
- **Manipulative**: Organizations with high economic performance concerns and low ethical concerns are called manipulative organizations. These organizations use tax laws, labour laws and union leaders to maximize profit.
- **Holistic**: Organizations with high ethical concerns and low economic concerns are called holistic organizations. These organizations spend their money in social and environmental purposes.
- **Balanced**: Balanced organizations have high ethical and economic concerns. These types of organizations gain profit as well as work for social and environmental purposes.

Figure 1.3 shows the different types of organizations classified by economic and ethical issues.

Ethical Issues



Economic Issues

Figure 2.1: *Different Types of Organizations*

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2.2.1 Corporate Code of Ethics

Corporate ethical codes can be defined as the standards and beliefs of an organization. These standards and beliefs are made by the managers of the organization. These ethical codes can be used to adjust the thinking and attitude of the individuals in the organization. Ethics codes of organizations are different from the rules of ethics. Ethical rules are the requirements according to which an individual acts.

Snoeyenbos and Jewell define three elements to implement ethical behaviour in the organization. These elements are:

- Implementing the corporate ethical code
- Introducing an ethics committee
- Introducing a management training programme that includes ethics training

Organizations can handle the issue of ethics by incorporating the code of business conduct in the corporate structure. These business codes can be used to advise, guide and regulate the behaviour of the individuals in organizations. Organizations can translate the human core values into business codes by using some specific guidelines. Many organizations have formulated codes of ethics for their employees. Most of these codes are very different and some are similar. These formulated codes of ethics can be used as a tool for developing ethical conduct. Some of the ethical codes formulated by organizations are:

- Ethical codes for discipline
- Proper code of dressing
- Avoiding abusive language or actions
- Punctuality
- Legalistic ethical codes
- Always following instructions from superiors
- Performance of fair performance appraisals
- Personal and cultural ethical codes

CHECK YOUR PROGRESS

1. What are the types of organization?
2. What are the three elements for implementing ethical behaviour in the organization?
3. Mention five ethical codes usually formulated by organizations.

- Not using official property for personal use
- Performance of good quality of work
- Having initiative
- Conservation of resources and protection of quality of environment

Advantages of a Code of Ethics

Some of the advantages of a code of ethics are:

- Code of ethics can be used to handle outside pressure.
- They can also be used in making overall strategic decisions.
- These codes can be used to define and implement the policies of the organization and distribute work between the employees.
- Code of ethics can be used to optimize the public image and confidence of the organization.
- They can be used to increase the skills and knowledge of the individuals.
- Code of ethics can also be used to respond to the different issues of stakeholders.
- These codes of ethics can be used to discourage improper requests from employees.
- They can also strengthen the enterprise system.

2.3 DEVELOPMENT OF ETHICAL CORPORATE BEHAVIOUR

The approaches to business ethics can be classified into the following areas:

- Identifying practical issues and assigning responsibilities
- Analysing existing practices and framing a code of conduct
- Raising fundamental philosophical problems

2.3.1 Identifying Practical Issues and Assigning Responsibilities

This approach explores various kinds of ethical issues that can arise in business and society. Business activities should be conducted in such a way that they do not cause any harm to the society. The various ethical issues that can arise in business and society are:

- Employee rights
- Ethical business conducts
- Environmental protection
- Child labour in business
- Discrepancies in the wages of women employees
- Bonded labour
- Exploitation of unorganized labour
- Minimum wages
- Obligations of large and multinational corporations

2.3.2 Analysing Existing Practices and Framing a Code of Conduct

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This approach deals with the subject of public policy and with the identification of unethical practices. There are various areas of conduct that require some amount of government regulation. Such areas include product liability, worker rights, environmental problems, white-collar crimes and child labour. This approach also deals with the ethical guidelines that provide benchmarking for the decision-making process.

Benchmarking

Benchmarking is one of the trends or perspectives that can be used by the management for the purpose of organizational development. Benchmarking can be defined as a process of comparing the works and service methods against the best practices and best outcomes. Benchmarking acts as a powerful agent for change and motivation that helps in organizational development. Benchmarking basically focuses on identifying changes that can result in higher-quality output by incorporating different organizational behaviour techniques. The process of benchmarking involves looking both inside and outside the organization for identifying the methods that can be used for organizational development. Benchmarking facilitates organizational development by identifying improvement strategies. It enables the organization to learn from other organizations. It also helps in the relocation of resources that speed up organizational development. Benchmarking is also used to train and develop human resources to ensure efficient performance that is comparable to the performance of competitors.

Benchmarking involves team activity. In benchmarking, a team activity should be encouraged by seeking new ideas, suggestions and cooperation through a process of external consultation. Benchmarking also involves introducing new ways of working that utilize the talents and abilities of the employees working in an organization. The active involvement of employees at all levels ensures their interest and commitment, which is essential for organizational development. In an organization, the internal teams which are used to obtain and analyse data related to benchmarking are responsible for recommending changes and improvements in order to support organization development. There are basically three types of benchmarking: internal benchmarking, functional benchmarking and competitive benchmarking. Internal benchmarking is carried out between closely related divisions or similar plants of the organization. This type of benchmarking uses shared performance parameters as a basis for comparison. Functional benchmarking is a more positive approach than internal benchmarking. Functional benchmarking is used to compare performance parameters of similar business units of different organizations. It is also used to compare various procedures followed by the organizations for the purpose of organizational development. Competitive benchmarking uses customer requirements as a parameter for comparing the performance of the organization against other companies that are best in the industry. This helps in identifying the areas which should be targeted for improvement, in order to ensure organizational development.

Some organizations implement benchmarking at the start of the projects. This strategy begins with the formation of a team, which is responsible for defining the goals of the project and identifying the areas in which benchmarking will be used.

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Other organizations use benchmarking to carry out their day-to-day activities. The examples include the development of benchmarking strategies to reduce manufacturing set up time, increase in the number of customers served per hour and cut in the delivery time. The following is the sequence of steps involved in an effective benchmarking process:

- Determine the key performance areas that need to be benchmarked. These include products and services, customers, business processes in all departments and organizations, business culture and calibre and training of employees.
- Identify the most relevant competitors and best organization in the relevant industry.
- Set the key standards and variables that need to be measured.
- Measure the standard variables regularly and objectively.
- Develop an action plan to gain or maintain superiority over competitors.
- Specify programmes and actions to implement the action plan and monitor the ongoing performance of the organization.

2.3.3 Fundamental Philosophical Problems

Under this approach, business ethics can be defined as an attempt to keep ethical obligations. This approach deals with the relationship of the individual and the society and it is used to identify the area of development of the society and its culture.

It also focuses on the differences between personal morality and social morality. The main aim of this approach is to identify and define business values.

Business values

A business value refers to a set of beliefs pursued by an organization. Business values like 'customer satisfaction', 'enthusiatic teamwork' and 'state-of-the-art provision for production' are some of the commonly pursued values by several organizations.

When such values are pursued effectively and with zeal by executing them in the daily activities of the management and the employees of the organization, they are believed to pay back in manifold returns and success.

Pursuing business values plays a vital role in the growth and survival tactics of an organization.

In general, the most common values that facilitate in improving profits and the image of the organization are as follows:

- **Persistent progress**: It refers to an eagerness and enthusiasm on the part of the organization to keep its functioning as an ever efficient and up-to-date working endeavour towards progress.
- **Customer satisfaction**: It refers to making the customers feel important and responding to their needs, interests and, if need be, providing solutions to their problems in case of any documentation processes regarding the purchase of the organization's product.
- **Personnel development**: When it comes to development, organizations can benefit more by developing the skills of their employees. Besides considering the satisfaction of its customers and management, it should

also take into account the satisfaction of its employees, which in turn can yield sincere work performance from the employees.

- **Innovation**: It refers to the enthusiasm to take on new challenges and responsibilities on the part of the employees and a desire to diversify and try out new ventures on the part of the organization.

Optimal use of resources: It refers to making sincere efforts to enhance overall business performance by maximum utilization of the organization's current resources.

2.4 ETHICAL LEADERSHIP

Importance of Leaders in an Organization

A leader is an integral part of an organization, because it is the leader who helps the organization to achieve the goals and objectives. The various reasons why the leaders are important for an organization are as follows:

- A leader acts as a friend to the employees he is leading.
- A leader recognizes the potentialities of the individuals and transforms them into realities.
- A leader wins the confidence of the employees of an organization.
- A leader unites the people as a team and builds up team spirit.
- A leader maintains discipline among his group and develops a sense of responsibility among them.
- A leader builds up a high morale among the employees of the organization.
- A leader motivates his group in order to achieve the goals and objectives of an organization.
- A leader maintains the ethical standards among the employees of an organization.
- A leader acts as a link between the work groups and the forces outside the organization.

Leadership is a form of management, and can be defined as the art of getting things done by others. Thus, the term management divides all the employees of the organization into two groups. These groups are:

- **Managers**: Managers are the individuals in the organization who are responsible for directing the activities of others.
- **Workers**: Workers are the individuals who are working under the control of the managers or leaders.

Leadership involves planning, organizing and controlling the resources of the organization so as to achieve the goals and objectives of the organization. The managers of the organization make some rules to coordinate and control their subordinates in the right manner. These rules can be determined by the environment and the culture of the organization. These rules also define the relationship of the managers with their subordinates and peers. These rules defined by the managers of the organization are termed as descriptive ethics because no one is forced to follow them. These rules are the contextual and moral guidelines that the managers derive from their personal moral philosophy. The moral awareness of the managers can be ascertained by the organizational administration.

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Management ethics in an organization deals with the morality and conduct of the individuals and the responsibilities of the management. Therefore, ethical management or ethical leadership deals with issues relating to managerial misbehaviour and the moral conduct of the management.

2.4.1 Ethical Issues in Organizations

There exist many different ethical issues in the organization or at the workplace. Some of them are:

- Identifying the conflict issues in the organization and trying to avoid them
- Deciding different methods to motivate employees
- Managing fairness in employee performance appraisals
- Protecting secret information of the organization
- Identifying the areas of interest of customers, employees, suppliers, owners and the staff
- Taking action against the reports of complaints in the organization
- Handling different problems of employees
- Taking corrective action against employees

Ethics management programmes are used by the organizations to manage ethics in their workplace. According to Brain Schrag, 'Ethics programmes convey corporate values using codes and policies to guide decisions and behaviour, and can include extensive training and evaluating, depending on the organization.' Ethics management programmes are made up of values, policies and activities that can affect the behaviour of the organization.

Managing ethics as a programme is advantageous to organizations in many ways. Some of the advantages are that:

- These programmes can assign an independent role to each individual in the organization to manage ethics.
- Ethics management can provide the necessary operating values and behaviour to the organizations.
- These programmes are used to align the operating values and behaviour.
- Ethics management programmes are used to schedule different ethical requirements.
- These programmes are used to make the organizations aware of ethical issues.
- These programmes provide structural mechanisms to handle ethical problems.
- They also provide some guidelines to decision-making.

2.4.2 Guidelines for Managing Ethics in Organizations

Some guidelines for managing the ethics in organizations are:

- **Identify ethics management as a process**: Ethics management is used to provide operating values and associated behaviour. Ethics programmes are process-oriented because the operating values are determined by ongoing reflection. The deliverables of the ethics programmes, such as codes, policies and procedures, budget times and meeting minutes, are not produced directly. However, these deliverables are produced by the process of reflection and dialogue.

- **Use ethics programmes to manage behaviour in organizations**: The ethical values provided by the ethical programmes can be used to direct behaviour in the workplace. Therefore, ethical management practices, in addition to ethical values, should also generate deliverables. These deliverables can be used to transform ethical values into behaviour.
- **Avoid ethical dilemma**: The codes of ethics and the codes of conduct can be used to minimize the occurrences of ethical dilemma.
- **Combine ethics management with other management practices**: Ethical management should be integrated with other management practices. While developing strategic planning, ethical values of the organization should be considered. While developing personnel policies, determine the ethical values that are most effective for the environment of the organization and then implement policies to produce these kinds of behaviour.
- **Develop ethics management programmes using cross-functional teams**: The employees of the organization should be included in the development and implementation of the ethics management programmes.
- **Value maintenance**: Ethics management programmes may increase the ethics of people in the beginning because of the sensitivity of people on their occurrence. However, people should remain ethical on the implementation of these ethics management programmes.

2.4.3 Roles and Responsibilities in Ethics Management

Each individual in the organization should be provided a specific role in managing ethics in the organization. However, the role assigned to each individual depends on the size and nature of the organization. The roles can also be full-time or part-time. The following responsibilities can be assigned in ethics management:

- The chief executive officer of the organization must support the ethics management programme.
- A committee or group should be developed in the organization to control the development and operation of the ethics management programme.
- A committee or group should be developed which should be responsible for training the employees on the policies and procedures of the ethics management programme and should resolve any ethical dilemmas that may arise. This committee can contain senior officers.
- A person in the organization should be designated as ombudsperson who has the responsibility of investigating or resolving complaints from the employees of the organization against the ethics management programme.
- Each person of the organization is responsible for the implementation of the ethics management programme.

2.4.4 Comparative Study: Japanese Management and Z Culture of American Companies

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Culture can be considered as a constellation of factors that are learned through our interaction with the environment and during our developmental and growth years. A growing baby learns a basic set of values, ideas, perceptions, preferences, concept of morality, code of conduct, and so on, through family and cultural socialization and such prevailing culture with which the member of the family is associated determines many of the responses that an individual makes in a given situation.

The organizational culture is a system of shared beliefs and attitudes that develop within an organization and guides the behaviour of its members. It is also known as 'corporate culture', and has a major impact on the performance of organizations, especially on the quality of work life experienced by the employees at all levels of the organizational hierarchy. The corporate culture 'consists of the norms, values and unwritten rules of conduct of an organization as well as management styles, priorities, beliefs and interpersonal behaviour that prevail. Together, they create a climate that influences the way people communicate, plan and make decisions. Strong corporate values let people know what is expected of them. There are clear guidelines as to how employees are to behave generally within the organization and their expected code of conduct outside the organization. Also, if the employees understand the basic philosophy of the organization, then they are more likely to make decisions that will support these standards set by the organization and reinforce corporate values.

The word 'culture' has been derived metaphorically from the idea of 'cultivation', the process of tilling and developing land. When we talk about culture, we are typically referring to the pattern of development reflected in a society's system of knowledge, ideology, values, laws, social norms and day-to-day rituals. Since the pattern of development differs from society to society, the cultural phenomenon varies according to a given society's stage of development. Accordingly, culture varies from one society to another requiring a study of cross-national and cross-cultural phenomenon within organizations. For example, Japanese work culture is very different from American work culture. In America, the ethics of competitive individualism shapes organizational management and operational performance. The industrial and economic performance in America is taken as a kind of a game in which each individual desires to be a 'winner' in order to receive a reward for successful behaviour. This work culture is a continuation of general culture and family upbringing where children are encouraged to 'think for themselves', and show a sense of assertion and independence.

The Japanese culture, on the other hand, encourages individuals as a part of a team, thus encouraging interdependence, shared concerns and mutual help. The organization is viewed as a family to which workers frequently make life-long commitments as they see the organization as an extension of their own families. The authority relations are often paternalistic in nature and strong links exist between the welfare of the individual, the corporation and the nation.

CHECK YOUR PROGRESS

4. What are business values?
5. Mention the guidelines for managing ethics is organization.

Origins of Organizational Culture

While culture has been a continuous development of values and attitudes over many generations, at least the organizational culture can be partially traced back to the values held by the founders of the organization. Such founders were usually dynamic personalities with strong values and a clear vision as to where they wanted to take their organizations. These founders usually selected their associates and their employees who had a similar value system so that these values became an integral part of the organization.

Second, the organizational culture is influenced by the external environment and the interaction between the organization and the external environment. For example, one organization may create a niche for itself for an extremely high quality defect-free product as a result of competitive forces and customer demand, while another organization may opt for moderate quality but lower prices. The work cultures of these two types of organizations would accordingly differ and would be influenced by external forces such as customer demand.

Third, work culture is also a function of the nature of the work and the mission and goals of the organization. For example, in a professional, research-oriented, small organization, the workers may be more informal at all hierarchical levels of the organization, the dress code may not be strictly observed and the employees may be encouraged to be independent and innovative. In contrast, other organizations may have a strictly enforced formal classical hierarchical structure with clearly established channels of communication and strict adherence to work rules. Accordingly, the organizational culture of these two types of organizations would be different.

Much has been written and talked about Japanese management styles. Almost invariably, the economic success of Japanese society is associated with Japanese culture. The cultural aspect of organizational performance came into focus with Theory Z, proposed by William Ouchi in 1981. Even though Theory Z draws heavily on the Japanese approach to management, it is more a combination of the current American as well as Japanese style of managing an organization. Basically, Ouchi’s approach to management calls for:

- Consensus decision making
- Worker participation in all phases of organizational operations
- Genuine concern for the overall well-being of employees
- Lifetime job security

The importance of strong culture as a driving force for organizational success was emphasized by Peters and Waterman in their well-received book, *In Search of Excellence.* They observed:

> ‘Without exception, the dominance and coherence of culture proved to be an essential quality of the excellent companies. Moreover, the stronger the culture and the more directed it was towards the marketplace, the less need there was for policy manuals, organization charts and detailed procedures and rules. In these companies, people way down the line know what they are supposed to do in most situations because the handful of guiding values is crystal clear.’

Some of the cultural differences in a typical American organization as compared to a typical Japanese organization can be seen in the following comparison in various areas and aspects of organizational operations and performance.

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Typical American Organization

- Usually, employment is short-term. Layoffs are quite common. Lateral job mobility is also common.
- Performance evaluations and promotions are relatively fast.
- Career paths are very specialized. People tend to stay in the same area, such as accounting, and become experts in their area.
- Decisions are carried out by individual managers who are responsible for the outcome of such decisions.
- The control systems are very explicit via policies, rules and guidelines and people are expected to strictly follow these guidelines.
- The organization is concerned primarily with the worker's work life and his role in the organization.

Typical Japanese Organization

- Fairly long-term, usually lifetime employment.
- Rigorous evaluation and slow promotion.
- People are primarily generalists and they become familiar with all areas of operations.
- Collective decision making is the norm.
- Primary reliance is on implicit control (self-control). People rely heavily on trust and good will.
- The organization is concerned with the whole life of the worker, business as well as personal and social.

These cultural views are so contrary to each other, even though both American as well as Japanese organizations are successful in their own ways. Theory Z essentially combines these two approaches and in most cases, it modifies American corporate culture to be more consistent with Japanese corporate culture. However, since total adherence to Japanese corporate cultural values such as lifetime employment and slow promotions can stifle creativity, dilute the intensity of challenges and restrict upward mobility, the modified Theory Z falls short of accepting the Japanese management style to replace the American style of management.

The modified Theory Z emphasizes the following aspects in relation to the specific areas of differences between the operating styles of a typical American organization and a typical Japanese organization as discussed earlier. These specific aspects are:

- Long-term employment and recycling of human talent through training: This will develop a sense of loyalty and dedication among workers.
- Relatively slow evaluation and promotion: The emphasis is more on training and enhancement of skills. Promotions are based on skills rather than seniority.
- Career paths are not highly focused in that a person acquires a variety of skills through job rotation and training so that he/she has a better feel of the entire organization rather than just his/her job.
- Control is both explicit and implicit. Self-control is encouraged along with respect for established policies and regulations.

- Decision making is by consensus, specially on those key issues that would affect the activities of the workers.
- Responsibility is not collective but is assigned to individual managers who are then held accountable for their decisions. They do have the authority to delegate some of their decision-making authority to their subordinates but the accountability still remains with the individual managers.

In addition to the work and performance of workers, the organization takes active interest in the worker's family and social life and provides facilities where social interaction among all members of the organization, irrespective of the rank, is encouraged.

While many of these factors are common to all successful organizations, such as participative decision making and encouraging team spirit by rewarding group efforts, some other factors are indeed culturally based and organizations must make decisions in accordance with their own unique culture.

2.5 SUMMARY

While management ethics concentrates on the ethical quality of management level decisions, organizational ethics considers the issues of morality and rationality in organizations.

Corporate ethical codes are used by organizations as a tool for developing ethical conduct.

2.6 ANSWERS TO 'CHECK YOUR PROGRESS'

1. Organizations can be classified into four types. These are:
   - Exploitative
   - Manipulative
   - Holistic
   - Balanced
2. Snoeyenbos and Jewell define three elements to implement ethical behaviour in the organization. These elements are:
   - Implementing the corporate ethical code
   - Introducing an ethics committee
   - Introducing a management training programme that includes ethics training.
3. Some of the ethical codes formulated by organizations are:
   - Ethical codes for discipline
   - Proper code of dressing
   - Avoiding abusive language or actions
   - Punctuality
   - Legalistic ethical codes

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4. A business value refers to a set of beliefs pursued by an organization. Business values like ‘customer satisfaction’, ‘enthusiatic teamwork’ and ‘state-of-the-art provision for production’ are some of the commonly pursued values by several organizations.
5. Some guidelines for managing the ethics in organizations are:
   - Identify ethics management as a process
   - Use ethics programmes to manage behaviour in organizations
   - Avoid ethical dilemma
   - Combine ethics management with other management practices
   - Develop ethics management programmes using cross-functional teams
   - Value maintenance.

2.7 EXERCISES AND QUESTIONS

1. Explain the advantages of a Code of Ethics.
2. What are the ethical issue that may exist in organization?
3. Explain the guidelines that help in managing ethics in an organization.
4. What are the types of organizations? Explain the classification.
5. What do you understand by ethical corporate behaviour?

2.8 FURTHER READING

Modh, Satish, *Ethical Management.*

Mathur, U.C., *Corporate Governance and Business Ethics.*

UNIT 3 ETHICAL DECISIONS

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Structure

3.0 INTRODUCTION

The management of an organization is responsible for making effective decisions. Managers are responsible for all business operations and they also make all the important decisions. To make decisions ethically correct, various models are considered for the purpose of good decision-making. There are various frameworks of decision-making based on factors such as duty, consequences and virtue. Managerial decision-making involves defining problems and then structuring them for positive results. There are certain steps to be followed during decision-making.

3.1 UNIT OBJECTIVES

This unit teaches you about:

- Decision-making, and the phases in the Simon decision-making model
- Problems in the decision-making process
- Factors affecting decision-making
- Concept of social responsibility of business
- Managerial roles and managerial skills in corporate governance
- Corporate governance models

3.2 ETHICAL DECISION-MAKING

Managers affect the behaviour and decision-making capability of individuals. The individuals in an organization are responsible for conducting business operations. Management is defined as a decision-making process. Ethical decision-making is a method of evaluating and choosing the alternatives decided by ethics management. The following should be kept in mind while making ethical decisions:

- Identify and eliminate unethical options in the alternatives.
- Identify complex, ambiguous and incomplete facts and try to avoid them.

- Determine the ethical dilemma and resolve it.
- Select the best ethical alternative.

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Organizations need to perform a set of activities and take various decisions to achieve organizational goals. These are known as the business strategies of the organization. Business strategies are an important part of businesses, firms and industries. To make a business strategy, all businesses, firms and industries need to develop a strategic plan once a year. Managers of the firms are given the responsibility to achieve the goals stated in the strategic plan. Business strategies are used for the following purposes:

- They help determine the products and services that an organization needs to provide.
- They help determine the various industries in which the organization competes.
- They help identify the competitors, suppliers and customers of the organization.
- They help analyse the long-term goals of the firm.

3.2.1 Simon Decision-making Model

Herbert A. Simon planned a model for decision-making that was known as the Simon's model of decision-making. According to Herbert A. Simon, the decision-making model is based on the following sequence of steps. These steps are:

(i) Identifying the problem

(ii) Generating alternative solution

(iii) Selecting a solution

(iv) Implementing and evaluating the solution

This model has the following three phases:

- The Intelligence phase
- The Design phase
- The Choice phase

The Intelligence Phase

A decision-maker gets to learn about the environment where a problem occurs. The scanning of environment may be continuous or irregular. For example, a review of daily scrap report by a production manager to check the problems related to quality constitutes continuous scanning, while frequent visits of a sales executive to the key customers to identify customer needs constitute irregular scanning. The intelligence phase of the decision-making process involves problem searching and problem formulation.

- **Problem searching**: In this phase, the difference between the expected and real result is obtained after making a decision that helps recognize the problem. The formula for problem searching is as follows:

  Deviation = Expected – Actual

  For example, a sales manager sets a sales target of five lakh in a particular month as his expected target. This target could not be achieved and only four lakhs worth of sales were made. Therefore, the difference between the expected and real value of the target helps recognize the problem in setting the target.

- **Problem formulation**: In this phase, the problem is identified properly to avoid the risk of solving the wrong problem. Here, the problem is clearly stated and well understood. If, sometimes, the problem is difficult to understand, it is broken down into smaller and manageable sub-problems. Also, sometimes, relationships are established with previously solved problems that help in solving the current problem.

The Design Phase

In this phase, various alternatives are developed in order to get the best possible alternative to solve a particular problem. The decision-maker makes a detailed analysis of each and every alternative before taking the final decision.

The Choice Phase

In this phase, an alternative, which was developed in the design phase, is selected. This selection helps the decision-maker in taking appropriate decisions. After making a decision, the decision is implemented. However, at any phase, the decision-maker may return to the previous phase. For example, the decision-maker in the choice phase may reject all alternatives and return to the design phase for developing new alternatives.

3.2.2 Types of Decisions

Organizational decisions can differ in different ways, which initiates development of different types of decisions from which organizations can choose the appropriate decisions. Organizational decisions are primarily classified on the basis of the purpose of decision-making. Knowledge of outcomes is another approach for classifying organizational decisions. An outcome defines what is going to happen if a particular decision is taken or a particular course of action is taken.

Organizational decisions involve selecting the best alternative from amongst the available alternatives. Organizational decisions are classified into the following categories:

- **Strategic planning decisions**: These are the decisions in which a decision-maker develops objectives and allocates resources for achieving these objectives. Decisions under this category are used for a long period of time and involve a large investment. For example, introducing new products and the acquisition of another organization are strategic planning decisions.
- **Management control decisions**: These are the decisions taken by the management control-level managers, who are at the middle level of the management hierarchy in an organization. These managers deal with the use of resources in the organization. The management control decisions include the analysis of variance, product mix and planning decisions.
- **Operational control decisions**: These are the decisions that deal with the day-to-day problems that affect the operation of an organization. For example, decisions such as production scheduling and inventory control

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fall under this category. Decisions under this category are taken by the operational-level managers, who are at the bottom-level of the management hierarchy in an organization.

- **Structured decisions**: These are the decisions that are well defined and require application and implementation of some specified procedure or decision rule in order to reach a decision. Such decisions require less time for developing alternatives in the design phase. Structured decisions are made by operating procedures or by using other accepted tools. More modern techniques for making such decisions involve operations research (OR), mathematical analysis, modelling and simulation.
- **Unstructured decisions**: These are the decisions which are not well defined and have no pre-specified procedure or decision rule. These decisions may range from one-time decisions relating to a crisis to decisions relating to recurring problems. The unstructured decisions usually consume much time in the design phase of the decision-making process. These decisions could be solved using judgement and intuition. Modern approaches to such decisions include special data analysis on computers and heuristic techniques. Such decisions are usually handled by strategic planning level managers because of their unstructured nature.
- **Semi-structured decisions**: These are the decisions that are neither structured nor unstructured. These decisions fall somewhere between the structured and unstructured decisions. For example, the introduction of a new product is a semi-structured decision.

3.2.3 Knowledge of Outcomes

The knowledge of outcome plays an important role when you have more than one alternative. On the basis of the level of knowledge of outcomes, decision-making can be classified into the following three categories:

- **Under certainty**: Decision-making under certainty takes place when the outcome of each alternative is fully known and there is only one outcome for each alternative. In such a situation, the decision-maker is required to compute the optimal alternative or outcome.
- **Under risk**: Decision-making under risk occurs when there is a possibility of multiple outcomes of each alternative, and a probability of occurrence can be attached to each outcome. Such decision-making is also similar to decision-making under certainty where instead of optimizing outcomes, a general rule is applied to optimize the expected outcome. A decision-maker is assumed to be reasonable for choosing a particular decision. For example, a decision-maker has to choose from two options, one offering a 2 per cent probability of a profit of Rs 1,00,000 and the other an 80 per cent probability of a profit of Rs 10,000. The decision-maker chooses the second alternative because it gives a higher expected value. This is explained by using the following formula:

```
Outcome x Probability = Expected Value
1,00,000 x 0.02 = 2,000
10,000 x 0.80 = 8,000
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- **Under uncertainty**: Decision-making under uncertainty takes place when there are many outcomes for each alternative and the probabilities of occurrence of the alternatives are not known. Decision-making under

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uncertainty arises when different people in an organization take decisions by applying different decision rules. For example, some may assign equal probabilities to all the outcomes for each alternative so as to treat the decision-making as 'decision-making under risk', whereas others may adopt different criteria, such as maximax and maximin criteria to minimize regret.

3.2.4 Characteristics of Good Decision-making

ider ifferent characteristics of a good decision-making are:

- Decision problems should be grabbed by the management both in space and time. This means, the decision problem should be analysed thoroughly by the management.
- The decision made by the decision-maker should keep him in a state of calm.
- Decisions made by the management should contribute to harmony in the organization.
- Self-interest and self-orientation should not come in the way of decision-making.

3.2.5 Problems in the Decision-making Process

There are various problems faced by a management in the decision-making process. These problems are:

- **Insufficient information**: It refers to the lack of information which affects the performance and quality of the management in an organization.
- **Insufficient knowledge**: It refers to the difference between available knowledge and the required information for the management to take a decision.
- **Lack of time**: It refers to the pressure on the management to make decisions. If time is limited, then the management needs to take hasty decisions.
- **Poor communications**: It leads to the problem that arises due to improper communication of information.

Other limitations of any management in the decision-making process are with respect to the inability of the human mind to handle available knowledge as also human behaviour.

3.2.6 Ethical Decision-making Frameworks

There are three frameworks for ethical decision-making. These frameworks are:

- Consequence-based decision-making
- Duty-based decision-making
- Virtue-based decision-making

Consequence-based decision-making

Consequence-based decision-making is a useful approach for decision-making managers. This approach is beneficial for all the persons who are affected by this approach. This requires an appraisal of the effects of decision-making and the

CHECK YOUR PROGRESS

1. What are the various phases of the Simon Decision-making Model?
2. List the various ethical decision-making frameworks.
3. What are the characteristics of a good decision-making?

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forecasting of outcomes. The effects of decision-making can be measured in various ways. These are:

- Financial costs and benefits
- Human happiness
- Organizational growth

The limitations of the consequence-based decision-making framework are:

- It is hard for the managers to guess the effects of the actions.
- This approach can reduce the ethics of economics.
- There exist conflicts in the thinking of different individuals in the organization.
- This approach does not care for human life.

Duty-based Decision-making

Duty-based decision-making approach is based on the categorical imperative statement of Kant. This approach states that one should do to others only that which one would want done to oneself. This approach focuses on the people. It also considers ethics of duty. Various limitations of the duty-based decision-making approach are given as:

- It is difficult to know the intentions of individuals.
- Feelings and emotions of individuals can also cause problems.
- Like the consequence-based decision-making approach, it also does not consider human life.
- It is very difficult to collect the intentions of individuals into a rule and test it for universality.

Virtue-based decision-making

Virtue-based thinking is where a person thinks about the appropriate virtue or good in a particular decision, such as honesty, generosity and justice. It has the following limitations:

- Applicable virtue of a person is dependent on his thinking and his surrounding environment.
- All the ethics related to virtue-based thinking are based on judgement rather than specific rules and regulations.
- Virtue is based on integrity of character.

Ethical decision-making models

Research on the actual irrational process of decision-making situations is limited. Ferrell and Gresham developed a multi-stage model with three principles of ethical decision-making, which are as follows:

- Individual factors
- Organizational settings
- Opportunity to act

Individual factors relate to the individual and his value system. Organizational settings refer to the environment that advances or prevents ethical actions.

Opportunity to act refers to the chances, if at all, of an unethical act on the part of the individual.

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In a decision-making process, it is essential to relate decisions regarding possible processes to ethical content. Ferrell and Gresham also designed a model consisting of four factors that affect ethical decision-making on perceived ethical problems, alternatives, philosophical evaluations and judgements. These factors are:

- Personal experience
- Organizational norms
- Industry norms
- Cultural norms

To some extent, these models look complementary as they try to examine the multiple influences on ethically hypothetical situations rather than on actual decision-making procedures.

3.2.7 Normative Framework

The application of normative theory explains ethical decision-making clarifying two important points. First, normative theory is idealistic and not designed for the purpose of explaining or predicting behaviour. As it is idealistic, it may not involve actual and practical situations. Second, using a normative approach lacks validity, because few decision-makers make normative theories from daily processes. The normative ethical framework may also neglect the situation where an individual possesses conventional ethical norms because of situational variables.

Within normative ethics, differences exist between the deontologists and the teleologists. They differ on the basis of the evaluation and concept of morality. In the case of deontologists, some actions are right from their origin or may be correct according to some formal principle. However, in the case of the teleologists, moral judgements are justified on the basis of references to the goodness of a purpose or the results of an action.

To arrive at a list of representative normative frameworks is a challenging task in itself. The framework must not be narrowly focussed as this may direct all the actions to short-term benefits. The following are the principles that are most commonly applied in ethical discussions:

- **Personal benefit**: This framework acknowledges the range to which any action provides benefits to an individual in question. It also acknowledges the right to life and the freedom of an individual over his/her actions or information.
- **Social benefits**: It acknowledges the need for actions that are beneficial to society.
- **Principle of neutralization**: It is utilized to diminish the possible impact of norm-violating behaviour.
- **Categorical imperatives**: This framework is based on the idea that an action is morally correct or wrong regardless of its consequences.
- **Duty**: An action is originally right because of the duty arising out of a stated or unstated value system.

- **Principle of justice**: It acknowledges the rights of the individuals, fair compensation and fair distribution of benefits.
- **Principle of lawfulness**: It does not let anybody violate law.

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The above principles depict the range of traditional normative framework and is derived from specific results and non-specific results. The first three principles are consequentialistic as they relate to consequences of an action which affects the individual as well as the society. The remaining are non-consequentialistic as they are derived from duty-based or right-based theories.

3.2.8 Managerial Decision-making

Decision-making and problem solving is a core functions of a management because it is an integral part of all other managerial functions such as planning, organizing, directing and controlling. It is also an integral part of life because life cannot be managed without making decisions. We are always faced with situations where we have to make choices almost every day of our lives and making a choice out of many options constitutes a decision. This decision may be a simple one, such as choosing clothes to wear, selecting food from a menu or deciding the general activities for the day or it may be a major decision such as changing a job or purchasing a house.

Rational decision-making and problem solving may be used interchangeably since a problem has to exist and a decision has to be made to solve such a problem. While most decisions indeed involve a problem, some decisions are part of routine and may not involve a problem. For example, decisions as to what to wear or which movie to see or whether to stay or go for swimming are routine decisions and simple choices among available alternatives, requiring common sense and simple qualitative judgement. Problem solving, on the other hand, is a much more vigorous process which requires rational inquiry based upon unemotional reasoning, identifying the problem, generating feasible solutions for it, choosing the best solution from the point of view of utility and then applying this solution to see if it works efficiently and effectively. In general, while decision-making results in a choice from many alternative courses of action, problem solving results in resolving the disparities between the desired performance and the performance actually obtained.

Decision-making is a complex mental exercise in reality. Some of the decisions we make are highly significant with highly important consequences. The more significant decisions very often need the exercise of considerable analytical judgement and the quality of such judgement is the backbone of successful decisions. These judgements must eliminate the root causes of problems that have necessitated such decisions. Ineffective decisions attack only the symptoms and are only cosmetic in nature. They may solve the problem on the surface or on a short-run basis, but in order to find a lasting solution, the problem must be attacked at its roots.

As we all face the future, its unpredictability brings to us certain situations that are unexpected and hence problematic in nature. As we grow older and share added responsibilities, we develop certain characteristics and some intuitional senses that help us solve some of these problems. Moreover, we also learn some techniques and methodologies through the acquisition of knowledge and skills, which assist us in solving certain types of problems. These problems require decisions that exist at personal, organizational and social levels.

Individuals must make major decisions regarding their careers, their marriage and family and other decisions, which have far-reaching personal implications. Organizational decisions involve problems relating to investments, products, marketing, location of production or service facilities, dealing with personnel problems, contributions towards community welfare, and so on. Societies, in general, have many problems that affect their very survival, such as crime, energy shortages, depletion of finite resources, health services, employment and political conflicts among nations.

All these problems have to be faced and solved. No person can avoid problems and ignoring a problem is never a solution. As Thomas J. Watson Jr put it:

> I never varied from the managerial rule that the worst possible thing we could do would be to lie dead in the water with any problem. Solve it, solve it quickly, and solve it right or wrong. If you solved it wrong, it would come back and slap you on the face and then you could solve it right. Doing nothing is a comfortable alternative because it is without immediate risk, but it is an absolutely fatal way to manage a business.

From organizational point of view, the decision-making process is such an integral and important part of management that some thinkers propose that management is simply a decision-making process. They call it the 'decision theory school of management'. The basic emphasis of this school is not on people or environmental variables influencing the management behaviour, but on the process of decision-making and the theory that all management thought could be built around it. According to Simon:

> A theory of administration should be concerned with the process of decision as well as with the process of action. Even if the decision-making is not the only skill required for effective management, it cannot be denied that in fact it is an essential and highly important skill. This skill is actively utilized in all other functions of management such as planning, organizing, directing and controlling. Hence, decision-making is widely acknowledged as the centre of executive activity in business and industry and is considered as the major criterion for the evaluation of an executive's administrative performance.

3.2.9 Defining a Problem

Since a problem must exist in order to make a decision for solving it, we must know what the problem is so that we can identify it when it shows up. Being aware of the problem is the first prerequisite for finding a solution. The Webster's Dictionary defines a problem as 'a question raised for inquiry, consideration or solution'. While this definition is not complete or self-explanatory in itself, a problem seems to exist when the symptoms of the outcome of an activity do not seem to conform to the expected outcome of the same activity as planned. For example, you are going to your office in the car and on the way, you get a flat tyre, then you have a problem since you did not expect this to happen. Similarly, if someone becomes ill, then this is a deviation from the norm of healthy living and this would constitute a problem and the sick person would seek a solution to the problem by going to the doctor.

Structure of problems

According to Harvey G. Brightman, problems may be of the following types:

1. **Ill-structured versus well-structured problems**: The ill-structured problems are unique, unpredicted and unprecedented situations. These problems are ambiguous and poorly understood and defy any cut-and-dry solution. These are generally 'one-shot' occurrences for which standard responses are not available and hence, require a creative process of problem solving which is specifically tailored to meet the requirements of the situation at hand. Such problems may involve the closing of a plant, buying or merging into a new company, starting a new business, and so on. Because the ill-structured problems do not have well-structured solutions, such solutions generally rely upon skill, intuition, creativity, experience and considered judgement and carry with them the consequences of diverse ramifications. The top-level management generally faces these problems because their environment is complex and is involved with high-level policy decisions.

   Well-structured problems, on the other hand, are clearly defined, routine, and repetitive and respond to standardized responses. They are familiar, complete and easily defined and analysed. These problems are generally faced by lower-level and middle-level managers who have, at their disposal, a set of rules, policies and procedures misses can be used to solve these problems, so that such problems do not have to be referred to superiors for solutions. For example, if a professor cuts too many classes, the chairperson of the department can use the prescribed rules to discipline him and the issue does not have to be referred to the president of the college. Similarly, if you buy some merchandise and it turns out to be defective, you can take it back for a refund. The management of the company has a well-structured set of rules and procedures to deal with the problem of making refunds for defective merchandise.

2. **Operating level versus strategic level problems**: Operating-level problems are generally well-structured problems encountered by the organization on a daily basis. For example, a newspaper shop owner has the problem of reordering the newspapers and magazines every day and he knows when to order and how much to order. Similarly, daily or weekly production levels, inventory levels or sales levels are set and known and standard solutions exist to solve any problems in these areas when they arise. These situations are not new or unique and do not involve any changes in organizational policies or procedures.

   On the other hand, strategic-level problems are unique and demand high-level managerial attention. These problems may involve changes in policies and are important in terms of actions taken or resources committed. While operating-level problems do not affect the survival of an organization, strategic-level problems do. Sometimes, if the operating level problems are left unattended, they may become strategic-level problems. For example, if no action is taken against a professor who habitually miss classes, this may affect other professors thus making it a morale problem for the college, which then would be considered a strategic-level problem.

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3. **Crisis versus opportunity problems**: Crisis problems develop suddenly and are totally unexpected at a given time. These may develop within the general framework of expectations that the management has prepared to some extent to handle these crisis situations. For example, a forest fire will create a crisis problem but the government and the community is generally prepared to fight the forest fire. Similarly, a major strike at the plant may not have been expected, but the management has generally made provisions to handle the situation. Solving crisis problems is reactive in nature and requires reacting quickly and aggressively to solve the problem. It may be achieved through task forces, which may try to mould crisis situations into familiar problems for which the solutions are known to exist.

   The opportunity problems are more challenging. These must be exploited for the betterment of the organization, For example, if an opportunity of a highly beneficial merger arises, and the organization fails to recognize the potential, it would be considered a lost opportunity. Similarly, a slightly increased rate of employee absenteeism may mean some deeper organizational problem and if the management does not recognise this opportunity to deal with the problem, this missed opportunity may blow up into a crisis. The central management handles both the crisis problems as well as the opportunity problems.

The problem pointers

First, how do we determine that there is a problem? Even if we know that there is a problem, how do we determine the extent and seriousness of the problem? According to Miller and Starr, there are certain characteristics that are attributes of problems. One main characteristic of a problem is the existence of a deviation between what was expected under a given set of conditions and what actually happened.

Before solutions can be found, the problems must be thoroughly and correctly diagnosed and the decisions concerning solutions to the problems must be dealt with, keeping in view the underlying factors other than the surface symptoms. For example, a doctor prescribing a medicine for a headache as a symptom without looking into the root cause of it will only provide temporary relief and not really 'solve' the problem. Accordingly, in properly defining a problem, we must ask some critical questions relating to it. Some of these critical questions may be:

- What type of problem is it?
- How large is the deviation from the norm?
- How quickly has this deviation been observed?
- What are the critical factors relating to the problem?
- Why do we want to solve this problem?
- Would the cost of solving the problem be justified?
- Who should solve the problem and what particular method is chosen to solve the problem?

These initial questions would indicate the extent of the problem so that we can become fully aware of it and grasp its significance.

It is very important that the problem be diagnosed as early and correctly as possible. For example, cancer, when detected in earlier stages, may be cured, but

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in advanced stages it can be fatal. The early awareness of the problem is the first prerequisite for dealing with it. However, sometimes we may not even know that there is a problem when in fact it exists until it is too late. Colon cancer, for example, does not have obvious symptoms for early detection so that the patient may not even know that he has it until it reaches an advanced stage. At other times, we may be aware of a problem but may not consider it serious enough to find a solution until it becomes a crisis. Some problems may hit us when their severity can no longer be ignored. For example, too many lives lost in car collisions may require legislation about seat belts in cars in order to solve the problem of death and injury in car accidents. Similarly, the destruction brought about by typhoons and hurricanes may indicate the problem of inadequate early warning systems.

Another problem pointer is a built-in signal in the process of operations so that whenever there is a deviation from the expected outcome, it gives out a signal. For example, the Internal Revenue Service computer will create and send a signal to alert an administrator if some tax deductions are excessive in a given tax form so that some action can be taken. Similarly, our organizational accounting system can be set up in such a manner that any change in the cash flow or demand, increases the cost per unit produced; excessive and delayed state of accounts receivables, excessive inventories at hand, and so on will attract the manager's attention quickly for an appropriate action.

Third parties, such as a user of a product or a consumer representative group points out some problems. The problem of toxic wastes almost became a crisis when various consumer groups started pointing out the problem of community health to the government agencies. The polaroid instant camera came into existence because of a 'consumer complaint', when the consumer happened to be the daughter of the instant camera inventor, who wanted to look at the pictures taken right away. Thus, if a product is faulty, it can be brought to the attention of the manufacturer. The Federal Safety Commission and Food and Drug Administration in America test products to see if they conform to the prescribed standards. If they do not, then there is a problem for which the solution must be found.

There are some problems that come to the surface due to sheer idle curiosity. The problem may not be a real one but may be considered a problem if solving it leads to better outcomes. Such a problem is not really the deviation between what is happening and what is expected, but a deviation between what is happening and what is actually achievable.

For example, when Fredrick Taylor applied scientific methods to production, the productivity improved tremendously so that there was really no problem in production except that the situation was made into a problem by asking, 'can we do it better?' Based upon this premise, some organizations are continuously involved in finding problems with existing methods in order to improve upon them.

In general, a problem exists whenever there is a difference between an actual situation and the desired situation. For example, if the total number of incoming students into a college suddenly goes down than what was expected, then this would pose a problem requiring administrative attention and solution.

3.2.10 Factors affecting Decision-making

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Some of the factors and personal characteristics that have an impact on decision-makers are described below. Some factors are more important at higher levels of management and others are more important at the lower levels.

- **Programmed versus non-programmed decisions**: As discussed earlier, in the types of problems that managers face, programmed decisions are made in predictable circumstances and managers have clear parameters and criteria. Problems are well structured and alternatives are well defined. The problems are solved and decisions are implemented through established policy directives, rules and procedures.

  Non-programmed decisions are made in unique circumstances and the results of such decisions are often unpredictable. Managers face ill-structured problems. These problems require a custom-made response and are usually handled by the top management. To start a new business, to merge with another business or to close a plant are all examples of non-programmed decisions. For example, when Steven Jobs and Stephen Wozniak introduced the first Apple microcomputer in 1978, they were not certain about the market for it. Today, Apple Macintosh computer is a major competitor to IBM computers.
- **Information inputs**: It is very important to have adequate and accurate information about the situation for decision-making; otherwise, the merit of the decision will suffer. It must be recognized, however that an individual has certain mental constraints, which limit the amount of information that he can adequately handle. Less information is as dangerous as too much information. Some highly authoritative individuals do make decisions on the basis of comparatively less information when compared to more conservative decision-makers.
- **Prejudice**: Prejudice and bias are introduced in our decisions by our perceptual processes and may cause us to make ineffective decisions. First, perception is highly selective, which means that we only accept what we want to accept and hence, only such type of information filters down to our senses. Second, perception is highly subjective, meaning that information gets distorted in order to be consistent with our pre-established beliefs, attitudes and values. For example, a preconceived idea that a given person or an organization is honest or deceptive, good or poor source of information, late or prompt delivery, and so on, can have a considerable effect on the objective ability of the decision-maker and the quality of the decision.
- **Cognitive constraints**: A human brain, which is the source of thinking, creativity and decision-making, is limited in capacity in a number of ways. For example, except for some unique circumstances, our memory is short term, having the capacity of only a few ideas, words and symbols. Second, we cannot perform more than a limited number of calculations in our heads and it is tough to compare all the possible alternatives and make a choice. Finally, psychologically, we are always uncomfortable with making decisions. We are never really sure if our choice of the alternative was correct and optimal until the impact of the implication of the decision has been felt. This makes us feel insecure.

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- **Attitudes about risk and uncertainty**: These attitudes are developed in a person, partly due to certain personal characteristics and partly due to organizational characteristics. If the organizational policy is such that it penalizes losses more than it rewards gains, then the decision-maker would tend to avoid the alternatives that have some chances of failure. Thus, a manager may avoid a potentially good opportunity if there is a slight chance of a loss. The personal characteristics of a decision-maker regarding his attitudes towards risk taking affect the success of the decision. The risk taking attitude is influenced by the following variables:
    A. ***Intelligence of the decision-maker:*** Higher intelligence generally results in highly conservative attitudes and highly conservative decision-makers take low risks. There are others who are more willing to take calculated risks if the potential rewards are larger and there is some chance of success.
    B. ***Expectation of the decision-maker:*** People with high expectations are generally highly optimistic in nature and are willing to make decisions even with less information. The decision-makers with low expectations of success will require more and more information to decide upon a course of action.
    C. ***Time constraints:*** As the complexity of the personal habits of the decision-maker and the complexity of the decision variables increase, so does the time required to make a rational decision. Even though there are certain individuals who work best under time pressures and may outperform others under severe time constraints, most people, by and large, require time to gather all the available information for evaluation purposes. However, most people under time pressure rely on 'heuristic approach', which relies on satisfactory rather than optimal decisions. This limit the search for additional information, considering few alternatives and few characteristics of alternatives and focusing on reasons to reject some alternatives. This approach may also be in use when the cost of gathering information and evaluating all such information is too high.
- **Personal habits**: Personal habits of the decision-maker, formed through social environmental influences and personal perceptual processes must be studied in order to predict his decision-making style. Some people stick to their decisions even when these decisions are not optimal. For example, Hitler found himself bound by his own decisions. Once he decided to attack Russia, there was no going back even when he realized that the decision was not the right one. Some people cannot admit that they were wrong and they continue with their decisions even ignoring such evidence, which indicates that a change is necessary. Some decision-makers shift the blame for failure on outside factors rather than their own mistakes. These personal habits have a great impact on organizational operations and effectiveness.
- **Social and cultural influences**: A major impact on the style of the decision-maker is made by the social and group norms. According to Ebert and Mitchell, social norm is '*an evaluating scale designating an acceptable latitude and an objectionable latitude for behaviour activity, events, beliefs or any object of concern to members of a social unit. In*

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other words social norm is the standard and accepted way of making judgements.' In the same way, cultural background and other social environment have fundamental impact on the decision-making style of a manager. As for instance, in the organizational system followed in Japan, a decision-maker makes a decision after taking into consideration the view of others involved in it. This method is influenced by culture and makes the implementation of the decision very easy, as everyone takes part in the decision-making process. On the other hand, in America, the decision-making style is usually individual based. This is done with the help of decision models and qualitative techniques.

3.2.11 Steps in Decision-making

All decisions involve a series of sequential steps that lead to a particular result. These steps are generally followed to make systematic, objective, analytical and unemotional decisions and some management scholars have called this process a 'rational decision-making process.' Figure 3.1 shows the steps in decision-making.

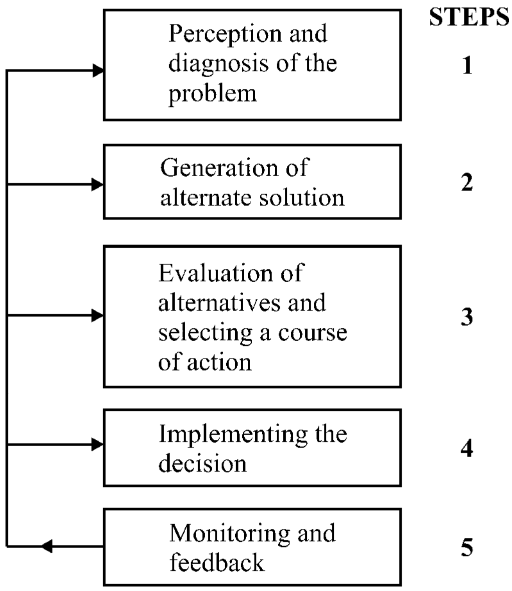

Figure 3.1: *The Decision-making Steps*

These steps are explained in more detail as follows:

1. **Perception and diagnosis of the problem**: Problems are defined in terms of discrepancy or deviation between the desired and actual state of affairs. The greater this deviation the more serious is the problem. This discrepancy must be perceived correctly, since any solution to a wrong problem would be a wrong solution. This deviation could develop either because the performance slips when the goals remain constant or because the goals change and the performance remains constant.

   A problem once isolated, must be defined and formulated. A written problem statement must be developed, describing as specifically as possible the nature and extent of the symptoms and when and where they occurred and what the underlying causes are thought to be. A written problem statement is easier to work on and more people can work on the

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problem at the same time. Furthermore, a written form provides an excellent form of communication to all parties concerned.

2. **Generation of alternate solutions**: The next step in decision-making process is to generate possible solutions and their consequences to the organization. All possible solutions should be considered because the most obvious solution may not be the optimal solution. However, creativity should be encouraged so that the focus can be shifted to unique solutions. The degree and depth of creativity would generally influence the quality of decisions and consequently the results of actions that are based on such decisions.

   Creativity must not be-locked by personal values or perceptions about the problem. It must be objective and removed from emotions and cultural taboos that might affect the outcome of a decision.

   While developing alternate courses of action, the decision-maker should take into consideration possible changes in the organizational environment as a result of the decision made and that might pose either a threat or an opportunity in a given period of time. In searching for alternatives, some of the resources that can be drawn upon are: the past experience of the decision-maker to look for similarities with the problems and solutions in the past, drawing on the experience of other experts both within and outside the organization and the responses of the people who would be affected by the decision.

3. **Evaluation of alternatives and selecting a course of action**: The evaluation of alternatives and selecting the best alternative with the most advantages is the most critical part of the decision-making process. A wrong choice would negate the effects of all efforts put in the preparation of the process. Finding the optimal choice requires the consideration of the possible impact of all alternatives in such a manner that the chosen course of action will not only meet the requirements of the objectives, but also eliminate the root cause of the problem. Some of the criteria against which the alternatives are to be measured are quantitative in nature such as return on investment, market share or net profits. Some other criteria are qualitative in nature such as consumer attitude, employee morale and ethics of the organizational mission. The bottom line in any decision criterion is the benefit derived from it in financial terms. This may be in the form of cost effectiveness, which means that for a given cost, the alternative with a greater degree of achievement of objective will be selected. Similarly, for a set level of achievement, the alternative with a lower cost will be accepted.

   No matter how tangible the methodology of the decision-making method may be, the effect of the personal judgement of the decision-maker in choosing the best alternative is always dominant. This judgement will be a reflection of current management values, ethics, social commitment and organizational politics. This judgement cannot be quantified and hence, must be based upon strong intuition and past experience.

4. **Implementation of the decision**: Implementation means putting the selected alternative into action and seeing it through to its completion. The process of implementation starts with assigning responsibilities to persons who will be involved in carrying out the decision. The possibility

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of any resistance to change should be examined, especially if it affects or conflicts with personal values and personalities and group norms or, as the case may be, group objectives. The implementation, of course, becomes easier if the persons implementing it and persons affected by it were also involved in the decision-making process and if they have some stake, financial or otherwise, in the success of the solution. It is vital to communicate the details of the decision and procedures for implementation to all the employees clearly, in detail, and in a manner that would invite commitment and dedication. This commitment can further be improved if the implementation plan has provisions for any necessary modification that may be required and the members of the organization should be empowered to modify the solution during implementation based upon their experience with it.

5. **Monitoring feedback**: Feedback provides the means of determining the effectiveness of the implemented decision. If possible, a mechanism should be built into the process, which would give periodic reports on the success of the implementation. In addition, the mechanism should also serve as an instrument of 'preventive maintenance' so that the problems can be prevented before they occur.

   In many situations, computers are very successfully used in monitoring, since the information retrieval process is very fast and accurate and in some instances, the self-correcting is instantaneous.

Monitoring the decision is necessary and useful irrespective of whether the feedback is positive or negative. Positive feedback reaffirms the correctness of the decision and the process. Negative feedback indicates either that the implementation requires more time, resources, efforts or planning than originally thought or that the decision was a poor one and needs to be re-examined.

3.3 ETHICAL DILEMMAS IN ORGANIZATION

There exist many different ethical issues in an organization or at the workplace. Some of them are as follows:

- Identifying the conflict issues in the organization and trying to avoid them
- Deciding different methods to motivate employees
- Managing fairness in employee performance appraisals
- Protecting secret information of the organization
- Identifying the areas of interest of customers, employees, suppliers, owners and the staff
- Taking action against the reports of complaints in the organization
- Handling different problems of employees
- Taking corrective action against employees

Ethics management programmes are used by the organizations to manage ethics at their workplace. According to Brain Schrag, '*Ethics programmes convey corporate values using codes and policies to guide decisions and behaviour, and can include extensive training and evaluating, depending on the organization.*' Ethics management programmes are made up of values, policies and activities that can affect the behaviour of the organization.

CHECK YOUR PROGRESS

4. List the factors affecting decision-making.
5. What are the steps in the process of decision-making?

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Managing ethics as a programme is advantageous to organizations in many ways. These are:

- These programmes can assign an independent role to each individual in the organization to manage ethics.
- Ethics management can provide the necessary operating values and behaviour to the organizations.
- These programmes are used to align the operating values and behaviour.
- Ethics management programmes are used to schedule different ethics requirements.
- These programmes are used to make the organizations aware of ethics issues.
- These programmes provide structural mechanisms to handle ethical problems.
- They also provide some guidelines to decision-making.

3.4 SOCIAL RESPONSIBILITY OF BUSINESS

Social responsibility of business involves the consideration of general public interest by businessmen while taking business decisions and actions.

According to Bowen, social responsibility refers to the '*obligations of businessmen to pursue those policies, to make those decisions or to follow those lines of action which are desirable in terms of the objectives and values of our society*'.

This entails that businessmen should perform their operations with due consideration to the aspirations of society. They should fulfil the demands of those who have a claim on the operations of business. They must measure the consequences of their decisions and courses of action on the society and ascertain that no undue harm is done to the interests of the society.

The concept of social responsibility has emerged due to several economic, social, political and legal influences. These forces, which have obliged, persuaded and helped businessmen to become aware of their responsibility to society, are as follows:

- **Public opinion**: Public interference with the help of the government has instilled a fear in the heart of businessmen. The threat of public regulation and public ownership has compelled them to acknowledge the fact that responsible behaviour is essential on their part for survival in the private sector.
- **Trade union movement**: The recent development of socialism that boosted the strength of labour unions has forced businessmen to give a fair share to workers. Human relations and labour legislation have facilitated trade unions to increase their influence.
- **Consumerism**: Consumer organizations have encouraged awareness about consumer rights. Consequently, businesses have become more responsive to consumer needs and stress the dictum of 'consumer is the king'. Businessmen can no longer adopt the approach of 'let the buyer beware'.

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- **Education**: Extensive education has made businessmen conscious about the quality of life, moral values and social standards. Liberal business leaders have been pressing the business community to acknowledge its social obligations.
- **Public relations**: Modern businessmen are aware that a good public image contributes to their growth. There is a greater alertness in their hearts that business is a construction of society and hence, it should consider and react positively to the expectations of society.
- **Managerial revolution**: Separation of ownership from control in large corporations has resulted in professionalism in management. A professional manager is fairly aware of the society's expectations and attempts to meet the demands of all social components, like customers, employees, shareholders and the government, in a well-adjusted manner.

The case of social responsibility has been subject of controversy since long. There have been arguments both in favour and against it. The main points that support the assumption of social responsibility by business enterprise are as follows:

- **Long-term self-interest of business**: As stated earlier, a good public image is bound to give better returns to a business enterprise. Businessmen can benefit in the long run by providing for the welfare of the society through education and better living conditions. This will result in better employees in business and enlightened customers in society who will benefit through their increased purchasing power.
- **Ascertainment of law and order**: Social responsibility on the part of business can avoid unrest in society. If the society feels that it is not getting its appropriate share in business, it is bound to create disorder by adopting anti-social and illegal activities and rebellions. Pursuing the doctrine of social responsibility can help business organizations prevent social chaos.
- **Maintenance of free enterprise**: Government or public regulation can hinder the development of business by decreasing the flexibility of decision-making and the freedom of choice and action. Therefore, the voluntary assumption of social responsibilities is essential for the growth of a business organization.
- **Creation of society**: Business is a part of society and survives on the demands of the society. Therefore, it should be responsive to social expectations and welfare. The right of the business to grow goes hand in hand with its awareness of social responsibility and welfare. It is the duty of the business enterprise to contribute in some way to the well-being of its society.
- **Moral justification**: Enlightened businessmen have now become more aware about their moral duty to serve the society. Business has the resources and power to solve social problems. Therefore, its power should be balanced with social responsibility.
- **Profitable environment**: To ensure a profitable environment in the society in which it operates, business needs to meet the challenges of social evils. Active interference on the part of businessmen in solving

these challenges can convert them to opportunities, which in turn will ascertain not just the existence, but also the benefits of the organization.

- **System interdependence**: Business system and social dependence are interrelated and thus affect each other.

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The arguments against social responsibility on the part of business enterprise are as follows:

- **Dilution of profit maximization**: Economic value is the main criterion by which the success of a business should be estimated. According to Milton Friedman, '*Few trends could so thoroughly undermine the very foundation of our free society as the acceptance by corporate officials of a social responsibility other than to make as much money for shareholders as possible. This is a fundamentally subversive doctrine. Management's spending for society is hypocrisy. Only people can have responsibilities not corporations*.'
- **Loss of incentive**: The motivation to utilize resources effectively is decreased when social responsibility is considered important. It is the profit motive principally that encourages optimum use of resources and manpower to run the business with enthusiasm.
- **Lack of standard**: Besides the effort motive, profit serves as a standard to measure the performance of business. A business organization goes off course as it loses the guiding measure that depicts the efficiency of its performance and thus hinders decision-making.
- **Business is an objective venture**: The emotional insights and experience essential to tackle social problems are lacking in the temperament of businessmen. They cannot determine what is in public interest. The solutions to social problems should be expected from specialized social agencies and not from businessmen.
- **Undue use of power**: If business organizations are involved in social institutions they are likely to dominate the decisions of these institutions for their own interests. They can use their financial power to take decisions concerning the functioning of these institutions. This may further lead to increased social detriment.
- **Market mechanism gets distorted**: The principle of social responsibility is based on the assumption that market mechanism is not the appropriate way to allocate scarce resources to alternative uses and so it should be replaced by political mechanism. If the market price of a product contains the cost of social actions, it does not actually represent the relative cost of producing it and thus the market mechanism gets distorted.

3.5 CORPORATE GOVERNANCE

Corporate governance is defined as an act of controlling, directing and evaluating the activities of an organization. The structure of corporate governance specifies that the others taking part in the organization, such as the board managers, board of directors, shareholders and other stakeholders must be provided with some rights and responsibilities. Providing powers to the participants of the organization results in the monitoring of performance of the employees in an organization. Corporate governance helps the organization achieve the goals and objectives of an organization in a desired manner.

Corporate governance has achieved a great deal of success in attracting public interest because corporate governance gives importance to the economic health of the corporation and the society as a whole. However, corporate governance covers a wide variety of the distinct economic phenomenon. Therefore, many people have given different definitions of corporate governance. A few definitions of corporate governance are as follows:

According to Shleifer and Vishny, 'C*orporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment.*'

An article from *Financial Times* has defined corporate governance as '*the relationship of a company to its shareholders or, more broadly, as its relationship to society*'.

According to the J. Wolfensohn, '*Corporate governance is about promoting corporate fairness, transparency and accountability*.'

3.5.1 The Need for Corporate Governance

There are various reasons for the need for corporate governance in an organization. These are:

- A corporation, which is a union of many stakeholders, such as employees, customers, investors, vendors, and so on, must be fair and transparent to its stakeholders in all its dealings. It is very important in today's globalized business world, where corporations require to have access to global pools of capital attract and retain the best human resource from all parts of the globe. If a corporation does not take up and show ethical conduct, it is not considered to be successful.
- Corporate governance covers ethical conduct in business, the code of values and principles that helps an individual to choose between right and wrong or make the right selection from the options or alternatives provided. Managers decide on certain actions on the basis of an principles that are governed by the culture, context and values of an organization. An organization that follows ethical values feel that it is better for the business, as it helps in the long run and the stakeholders observe that the management is running the organization in the desired way.
- It is beyond the sphere of law, i.e., it stems from the background and outlook of the management and cannot be regulated by legislation alone. It deals with running the affairs of a company in such a way that it is fair to all the stakeholders and that its dealings benefit the greatest number of stakeholders. It is about honesty, integrity and responsibility. Laws should set up a common framework to maintain standards. Since substance is very much linked with the mindset and ethical standards of management, it shall in the end lay down the creditability and integrity of the process.
- Corporations should realize that it is necessary for all the stakeholders to cooperate in order to facilitate development. Such cooperation and

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support can only be possible by adhering to the best practices of corporate governance. In this context, management has to take the responsibility of the shareholders at large and stop any unbalanced benefits of the varied sections of the shareholders.

- The economic competence of a company can be improved through corporate governance. Corporate governance also ensures that corporations consider the interests of a wide range of constituencies and also of the communities within which they function. Corporate governance also makes sure that the boards of directors are responsible to the shareholders. This even helps to ensure that corporations work for the benefit of the society at large, including the society's concerns about labour and environment.
- If the execution of good governance fails, heavy losses can result in terms of cost other than regulatory problems. Many organizations that do not give due importance to corporate governance end up paying a large risk premium while contending for scarce capital in the public markets. Of late, stock market analysts have started realizing, accepting and appreciating the relationship between returns and corporate governance.
- The confidence of both foreign and domestic investors is maintained and upheld due to the trustworthiness that comes from good measures of corporate governance. The cost of capital should be brought down so that more long-term investment is attracted.
- Often, importance and attention is given to corporate governance in times of financial crisis. In the US, when scandals disturbed the otherwise calm and contented corporate environment, new initiatives thrown up by them led to fresh debates in Asia and the European Union. With many instances of corporate misdemeanour coming into limelight, the emphasis now is on compliance with substance, rather than on form. It has also brought to the fore the need of intellectual honesty and integrity. The financial and other disclosures made by firms are only as good as the people who make it.
- In 1998, the Confederation of Indian Industry (CII) made public a desirable and voluntary code. This marked the beginning of corporate governance initiatives in India. Then, on the basis of the Kumarmangalam Birla Committee Report in February 2000, Securities and Exchange Board of India (SEBI) made the first formal regulatory framework for listed companies.
- Corporate governance has been defined in different ways. Many definitions do not give its scope and the motives of many of the definitions vary. However, the crux is that corporate governance is a concept and not an individual instrument. It encompasses necessary management and control structures of a company, the rules about the power relationship between owners, the board of directors, stakeholders and others. The easiest definition of corporate governance has been given by the Cadbury Report. It has been paraphrased as, 'the system by which

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business are directed and controlled'. The other all-inclusive definition has been given by the OECD (Organization for Economic Cooperation Code). According to it, corporate governance includes complex relationships among the management, its shareholders, board and others. It also establishes the framework through which the aims of the company are established and the methods of attaining those objectives and observing the working are decided.

- Corporate governance is aimed at increasing the long-term value of an organization for not only its shareholders, but also partners. It represents an amalgamation of all those involved in a process that is socio-economic. It is imperative for all organizations to govern and manage. Corporate governance includes the entire stakeholder and at the same time the process is economic as well as social.
- Studies related to corporate governance practices conducted worldwide by various institutions clearly indicate that no single model is available for good corporate governance. The OECD also recognizes this. It also accepts the fact that a wide range of approaches to corporate governance have developed due to the differences that exist in institutional frameworks, legal systems as well as traditions in various countries. All good corporate governance regimes place high preference on the interests of shareholders, as the latter place their trusts on corporations to use their investment funds in an effective and wise manner.

3.5.2 Principles of Corporate Governance

Corporate governance includes principles such as honesty, trust, integrity, responsibility, accountability and commitment to the organization. Apart from these, the other principles of corporate governance are as follows:

- **Rights and equitable treatment of shareholders**: The organizations must acknowledge the rights of the shareholders and they must help the shareholders in exercising their rights effectively. Shareholders must also be encouraged to participate in the general meetings of an organization.
- **Interests of other stakeholders**: It is the duty of an organization to recognize the legal and other obligations of certain stakeholders.
- **Role and responsibilities of the board**: In order to deal with various issues of a business, an organization needs a wide range of skills among the members of the board. The members of the organization must work with great responsibility.
- **Integrity and ethical behaviour**: In order to promote ethical and responsible decision-making, organizations must develop a code of conduct for the directors of an organization.
- **Disclosure and transparency**: The roles and duties of directors must be clearly defined by an organization. Organizations must implement certain procedures in order to verify and safeguard the integrity of the

organization. An organization must disclose the financial information to investors and shareholders.

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3.5.3 Role of the Board of Directors in Corporate Governance

Board of directors is made up of individuals elected by a corporation's shareholders to oversee the management of the corporation. An organization allows different individuals or parties to add to the capital, expertise and their knowledge so that the organization can function efficiently without facing any difficulties. There are various participants in the organization such as investors and shareholders. They do not participate in the operations of the organization. Their main interest is to have a proportion of the share in the income of the organization. The shareholders and investors have the right to elect the board of directors of an organization in order to represent and protect their interests. The board of directors has the power and duty to form the corporate policies of an organization. Therefore, the board of directors has the powers to take certain decisions, which can in turn affect the long-run performance of the corporation. It means that the board of directors has a very significant function in the working of the business as it also oversees the top management of the organization.

The duties and rules that the board of directors has to follow are plainly laid down by the organization. It includes monitoring the performance of the company and its management and approving important business policies. The board of directors is fully briefed in advance of board meetings and the matter that will be discussed in the meeting. The board of directors receives regular reports on the financial position of the organization, key areas of the organizations' operations and other issues.

The board of directors provides multi skills and knowledge to the organization and it also participates fully in making decisions on key issues that the organization faces. The organization follows its own performance review process to access how well the board and its committees are performing and how they might be further improved.

Responsibilities of the board of directors

The board of directors has to handle a wide variety of roles and responsibilities. There are certain laws and standards that define the responsibilities of the board of directors. These laws and standards differ from country to country. For example, the US does not have any laws and standards that the board of directors must comply with. The various responsibilities of the board of directors are as follows:

- Providing continuity to the organization by setting up the organization as per the legal requirements and effectively advertising its products and services to the customers.
- Selecting and appointing a chief executive whose basic duty is to review and evaluate the performance of the organization and offering administrative guidance to the organization.

- Governing the organization by setting up broad policies and objectives and monitoring whether the organization follows the policies.
- Acquiring the resources and finance for effectively running the day-to-day operations of the organization.
- The board of directors must be accountable to the public for the products and services of the organization, which include approving the budget and formulating the policies related to the contracts for producing a product.

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In legal terms, the main duty of the board is to direct the affairs of the organization but not to manage them. If the board of directors does not perform its responsibilities in the right manner and if it harms the organization in any manner, then the directors can be held responsible for the harm that is caused by them. Section 291 of the Companies Act had specified some of the general powers of the board and they are as follows:

- According to the provisions of the Companies Act, the board of directors is allowed to exercise the following powers within the organization:
    - o The board will do only those things which are directed by the management of the organization. The board must also assist in doing the things that are not mentioned in the clause of the Companies Act.
    - o The organization will abide by the provisions that are in the Companies Act and will also follow the provisions that are formed in the general board meeting of the organization.
- The company cannot make any regulations in the general meeting of an organization to invalidate any act of the board.

New trends of the board of directors in corporate governance

The board of directors plays a very important part in an organization. If a company possesses very good corporate governance and board of directors, then it will induce the investors to invest more in the organization. Investors are willing to invest more in an organization because good governance and the board of directors in an organization lead to better performance of the organization. Further, good governance reduces the chances of the organization falling into trouble. The various trends of the board of directors in corporate governance are as follows:

- There is more participation of the board not only in evaluating the performance of the company, but also in formulating the plans and policies of the organization.
- Institutional investors such as pension funds, mutual funds and insurance companies actively participate in the functioning of the board and they put pressure on the board to improve the performance of an organization.
- Non-management directors, which is not recognized in the eyes of law, are now actively participating in the board of an organization.

CHECK YOUR PROGRESS

6. Define corporate governance.
7. Who comprises the board of directors?

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- The number of the board members is reducing nowadays. This is because organizations prefer directors who have good knowledge and expertise rather those with general experience.
- As more and more organizations operate their services globally, they look for board members who possess international experience.

Role of top management in corporate governance

The board of directors occupies the top management whose prime concern is startegic management of the organization. The top management is supervised by the president in coordination with the vice-president of the organization and the vice-presidents of divisions and functional groups.

3.5.4 Responsibilities of Top Management

The responsibility of the top management is to get the objectives of an organization accomplished within the organization and in the industry. Thus, the role and responsibility of the top management is multifaceted and is directed towards the welfare of the organization. The duties of the top management are distinct as they may vary from organization to organization. The development of the tasks of the top management are developed by the analysis of objectives, strategies and fundamental activities of the organization. These tasks are divided among different levels of the top management staff which leads to diversity in skills. The analysis of this diversity in the top management team can be significantly related to improvements in the market share and profits of the organization. The top management should primarily support two critical responsibilities, crucial for strategic management to be effective. The two responsibilities are as follows:

- **Provision of executive leadership and strategic vision**: Executive leadership means directing the activities of the organization to accomplish its objectives. Strategic vision refers to the description of the capabilities of the organization, which is generally described in the mission statement. The top management defines the strategic vision of the organization to the employees. The enthusiasm and passion for the organization comes from the top management. Top management must have clear strategic vision, enthusiasm and dynamism. They possess three important characteristics that enable them to command respect and alter the process of strategy formulation and its implementation:
    - o ***Articulation of strategic vision with strategy***: The top management visualizes the organization as what it is expected to become and not to what it already is. He adds a new aspect to the strategic activities that enables the employees to refresh their working habits to attain new heights.
    - o ***Makes guidelines for others to identify and follow***: The behaviour of the top management towards the values concerning the objectives of the organization should be clear and must be communicated constantly through his work and activities. If the

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top management behaves responsibly then the employees trust in him and get inspired to work with the same enthusiasm.

- o ***Communicate high performance level and confidence to the followers**:* Leadership of the managers of an organization involves setting up of goals for the employees accompanied with challenges and training his people for the same. He should provide his workforce with power and resources before setting targets.

- **Manage strategic planning process**: In an organization, the characteristics of strategic planning are same as that in learning organizations where ideas can come from any division of the organization. Top management should encourage the planning process so that strategic management can work effectively in the organization. In multidivisional organizations, the top management should ask its units to prepare a strategy for themselves, which should be considered before planning and formulating the final strategic plan. Such practices make the work atmosphere dynamic and encourage the workforce to work according to their potential. The other method is to provide the workforce units with the mission statement and objectives and allow them to formulate strategies accordingly. Regardless of the approach taken to formulate a strategy, the board of directors expects the top management to prepare such a strategic plan that works well with the organizational objectives. Therefore, the top management's responsibilities include evaluating each unit's proposed objective, planning strategies to seek how effectively it satiates the organizational goals with respect to available resources and providing feedback.

3.5.5 Role of the CEO in Corporate Governance

Any action that is taken by any individual in the organization can affect the firm's operations to a great extent. For example, if any individual is appointed as a team leader, then he has the responsibility to take certain decisions that would help in the progress of his entire team. If an individual is provided with any sort of power, then it is up to him to use it for the benefit of the organization or he can use the powers to fulfil his own requirements. It is the same for CEOs in an organization. Organizations achieve great success in business because of their chief executive officer (CEO). The CEO oversees the company's finances and strategic planning.

The powers of a CEO can greatly influence the working of an organization. Therefore, it is very important to know about the powers of the CEO and how his powers can ultimately influence the results of an organization. The CEO of an organization has a very important role to play in certain areas of the organization, which are:

- Personal action
- Handling of organizational politics

- Role as a negotiator
- Role as a communicator
- Role as a role model

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Personnel action

The CEO of a firm has the power to take personnel actions in a manner that is beneficial for an organization in the following ways:

- ***Ordering the employees****:* A CEO of an organization uses his authority to order the employees. The employees of an organization are directed by a CEO to perform certain tasks at a defined period of time. If any of the employees are disobedient or their actions are not very good, then the CEO has an authority to throw him out of the organization. The ordering of employees is done to achieve the goals and objectives of an organization.

  The ordering method, which is employed by the CEO, provides certain benefits to the organization. When there is a need of any structural changes to be made in the organization, then the ordering method is very helpful. For example, if an organization decides to implement a new and improved structure for managing the performance of the employees in the organization, then the CEO has to just give instructions and train employees in operating the new system.
- ***Making cultural changes****:* It is very difficult for a CEO to change the culture of an organization. Cultural changes are those changes that are deeply rooted among the employees such as collective thinking, and mindsets, which have become a part of the organizational's working environment. For bringing about cultural change in the organization, just ordering the employees will not help the CEO. A CEO has to use the right approach for bringing about a change in the cultural mindset of the employees. For bringing about a change, a CEO must look after certain agendas and the communication network of an organization. If he finds any defects in the agendas or the communication network, then he must rectify those defects in order to make cultural changes among the employees and achieve the goals and objectives of the organization.
- ***Persuading the employees****:* A CEO of an organization persuades the employees to perform certain tasks in an efficient manner. If the employees find it difficult to perform certain tasks, then the CEO looks after the problems that the employees face in performing those tasks. After looking at all the difficulties, a CEO must persuade the employees to work better and direct their efforts towards the achievement of the goals. A CEO also negotiates with the employees if there is a situation of dispute between the employees and the management.
- ***Inducing the employees****:* A CEO also induces the employees to work towards the attainment of the goals and objectives of an organization. There may be certain employees in an organization that may not be performing well in accordance with the expectations of the organization.

A CEO can induce the employees by asking them to change their ways of working and thinking, so that organizational goals can be achieved in a desired manner.

Handling of organizational politics

The CEO must accept the fact that politics is certain in every organization. Pfeffer has defined politics as 'those activities taken within organizations to acquire, develop and use power and other resources to obtain one's preferred outcomes in a situation in which there is uncertainty or dissension about choices'.

Pfeffer further notes, 'If power is a force, a store of potential influence through which events can be affected, politics involves those activities or behaviour through which power is developed and used in organizational settings.' While power is a property of the system at rest, politics is the study of power in action. An individual, subunit or department may have power within an organizational context at some period of time; politics involves the exercise of power to get something accomplished, as well as those activities, which are undertaken to expand the power already possessed, or the scope over which it can be exercised.

Therefore, it is clear that political behaviour is designed and started to surmount opposition or resistance. If there is no opposition, there is no need for politics. Opposition and resistance are bound to occur in all organizations because of severe competition for scarce resources. Five major reasons that have strong influence on the political orientation of organizations are:

- ***Scarcity of resources****:* Any person or subunit having control over the allocation of scarce resources; their power and political influence play an important part in how these resources will be distributed to various departments, rather than fulfilling their own needs.
- ***Non-programmed decisions****:* Non-programmed decisions involve unique problems that cannot be solved by structured methods and procedures. These unique problems involve many factors and variables that are ambiguous in nature leaving room for political planning by those who have the knowledge and techniques to successfully confront and solve such complex problems. Such non-programmed decisions are likely to be made in the areas of strategic planning, mergers and acquisitions and policy changes.
- ***Ambiguous goals****:* When the goals of an organization are clearly defined and each member of the organization is aware of these goals and is also aware of his role in contributing towards the achievement of such goals, then there are limited grounds for political influences. However, when the goals of a department or the entire organization are ambiguous then there is more room available for playing politics.
- ***Technology and environment****:* An organization must have the ability to appropriately respond to an external environment that is highly dynamic and generally unpredictable. The organization must adequately adapt to

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complex technological developments that are changing day by day. Therefore, the political behaviour in organizations is increased when the internal technology is complex and when the external environment is highly unstable.

- ***Organizational change***: Whenever there are changes in the organizational structure or the rearrangement of organizational policies, individuals in powerful positions have the opportunity to play political games. These changes may include restructuring of a division or creation of a new division, personnel changes and introduction of a new product line. All these changes are invitations to political processes when various individuals and groups try to control the given situation.

All the above reasons apply to most organizations because the resources are continuously becoming scarce and competitive and the ever-changing technology makes the environment more complex to handle, which requires organizations to continuously evaluate their goals and strategies. This would make most organizations political in nature so that managers in responsible positions must become sensitive to political processes in order to play their role in acquiring and maintaining political power.

There can be politics among the different departments in an organization. For example, the research and development department of an organization requires Rs 5,00,000 for testing the new instrument and, on the other hand, the maintenance manager also requires Rs 5,00,000 for replacing an old pipeline. This puts CEOs in great difficulty in deciding to whom to allot the money. If the CEO gives 50 per cent of the money to both the departments, then both the departments will not be satisfied and will blame the CEO if anything goes wrong in the organization. Therefore, in order to minimize these problems, a CEO has to perform the following steps, which are:

- A CEO must sit with the two managers and with an open mind listen to their problems. The managers and the CEO must appreciate each other's viewpoints. By appreciating the views of both the managers, a CEO arrives at a particular figure that he will be able to meet the requirements of the managers.
- If the CEO finds that the demands of both the managers are urgent, then he will try to meet the demand by further borrowing the money from the finance department of the organization.
- If is not possible for the CEO to implement both the above options, then he must inform the managers that they have to use alternative methods and as soon as the finances are available they would be given to them.

Role as a negotiator

The CEO performs the role of a negotiator in which he has the full support of an organization. A CEO negotiates the problems that the employees face in performing the tasks in a specified period of time. If the CEO is busy in performing some other tasks, then the role of negotiator can be delegated between the general manager and any other departmental head. A CEO must keep some factors in mind before performing the negotiations:

- If the demands of the two persons cannot be met, then the person who is shouting should not get what he wants. If the demand of a person who was shouting more is fulfilled then it will lead to the belief that the demands of the person who shouts will be fulfilled. Therefore, to mitigate these problems, a CEO must patiently hear the problems or demands of the employees and must arrive at a situation that is acceptable by all wholeheartedly.
- A CEO must negotiate the problems in such a manner that the employees of an organization agree to increase the productivity and reduce the absenteeism.

Role as a communicator

A CEO plays the role of a communicator in an organization. It is an important duty of a CEO to communicate the organizational mission, vision, goals and objectives to the employees. The CEO, while playing the role of communicator, must listen to the employee's complaints and problems. A CEO must understand the problem first and then respond in a positive manner to the satisfaction of the employees who are facing the problem. Right communication given correctly at the desired time can motivate the employees and can charge them to perform the most difficult tasks with great ease.

Role as a role model

The CEO of an organization sometimes becomes a role model for the employees of the organization. The employees try to emulate the working style of the CEO. For example, if a CEO of an organization comes late, then the employees will follow him and they will also start coming late. On the other hand, if a CEO is punctual, then the employees will also be punctual. Therefore, the CEO has a great deal of influence on the employees and he must remain perfect in his actions.

3.5.6 Managerial Roles in Corporate Governance

The managers of an organization also play a very important role in the success of an organization and corporate governance. An organization must examine the roles that the managers are expected to perform. Henry Mintzberg developed these roles in the late 1960s after a careful study of executives at work. All these roles in one form or another deal with people and their interpersonal relationships. These managerial roles are divided into three categories. The first category of interpersonal roles arises directly from the manager's position and the formal authority bestowed upon him. The second category of informational roles is played as a direct result of interpersonal roles and these two categories lead to the third category, that of decisional roles. Figure 3.2 shows the various managerial roles.

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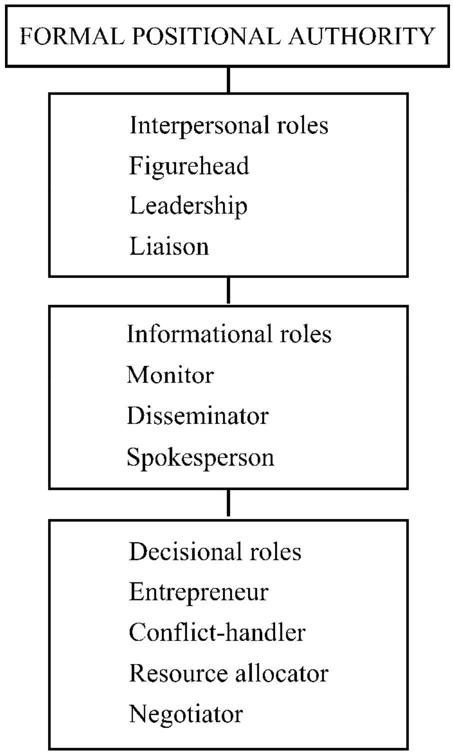

Figure 3.2: *Various Managerial Roles*

Interpersonal roles

Managers spend a considerable amount of time in interacting with other people, both within their own organizations as well as outside. These people include peers, subordinates, superiors, suppliers, customers, government officials and community leaders. All these interactions require an understanding of interpersonal relations. Studies show that interacting with people takes up nearly 80 per cent of a manager’s time. These interactions involve the following three major interpersonal roles, which are:

- **Figurehead**: Managers act as a symbolic figurehead performing social or legal obligations. These duties include greeting visitors, signing legal documents, taking important customers to lunch, attending a subordinate’s wedding and speaking at functions in schools and churches. All these, primarily, are duties of a ceremonial nature but are important for the smooth functioning of an organization.
- **Leader**: The influence of a manager is most clearly seen in his role as a leader of the unit or organization. A manager is responsible for the activities of his subordinates, he must lead and coordinate their activities in meeting task-related goals and he must motivate them to perform better. He must be an exemplary leader so that his subordinates follow his directions and guidelines with respect and dedication.
- **Liaison**: In addition to their constant contact with their own subordinates, peers and superiors, the managers must maintain a network of outside contacts in order to assess the external environment of competition, social changes or changes in governmental rules, regulations and laws. In this role, the managers build up their own external information system. In addition, they develop networks of mutual obligations with other

managers in the organization. They also form alliances to win support for their proposals or decisions. The liaison with external sources of information can be developed by attending meetings and professional conferences, by personal phone calls, trade journals and by informal personal contacts within outside agencies.

Informational roles

By virtue of his interpersonal contacts, a manager emerges as a source of information on a variety of issues concerning the organization. In this capacity of information processing, a manager executes the following three roles:

- ***Monitor**:* Managers are constantly monitor and scan their environment, both internal and external, collect and study information regarding their organization and the outside environment affecting their organization. This can be done by reading reports and periodicals, by asking their liaison contacts and through gossip and speculation.
- ***Disseminator of information**:* Managers must transmit the information regarding changes in policies or other matters to their subordinates, their peers and to other members of the organization. This can be done through memorandums, phone calls, individual meetings and group meetings.
- ***Spokesperson**:* A manager has to be a spokesman for his unit and he represents his unit in either sending relevant information to people outside his unit or making some demands on behalf of his unit. This may be in the form of the president of the company making a speech to a lobby on behalf of an organizational cause or an engineer suggesting a product modification to a supplier.

Decisional roles

On the basis of the environmental information received, a manager must make decisions and solve organizational problems. In that respect, a manager plays four important roles, which are:

- ***Entrepreneur**:* As entrepreneurs, managers are continuously involved in improving their units and facing dynamic technological challenges. They are constantly on the lookout for new ideas for product improvement or products addition. They initiate feasibility studies, arrange for capital for new products if necessary and ask for suggestions from the employees for ways to improve the organization. This can be achieved through suggestion boxes, holding strategy meetings with project managers and research and development personnel.
- ***Conflict handler**:* Managers are constantly involved as arbitrators in solving differences among the subordinates or the employee's conflicts with the central management. These conflicts may arise due to demands for higher pay or other benefits or these conflicts may involve outside forces such as vendors increasing their prices, a major customer going bankrupt or unwanted visits by governmental inspectors. Managers must anticipate such problems and take preventive action if possible or take corrective action once the problems have arisen. These problems may also

involve labour disputes, customer complaints, employee grievances, machine breakdowns, cash flow shortages and interpersonal conflicts.

- ***Resource allocator**:* The third decisional role of a manager is that of a resource allocator. Managers must establish priorities among various projects or programmes and make budgetary allocations to the different activities of the organization based upon these priorities. They assign personnel to jobs, allocate their own time to different activities and allocate funds for new equipment, advertising and pay raises.

All these roles are important in a manager's job and are interrelated even through some roles may be more influential than others, depending upon the managerial position. For example, sales managers may give more importance to interpersonal roles, while the production managers may give more importance to decisional roles. The traits of effective managers are their ability to recognize the suitable roles to play in each situation and the flexibility to change roles when required. However, managerial effectiveness is determined by how well the decisional roles are performed by the manager in the organization.

3.5.7 Managerial Skills in Corporate Governance

A manager must possess certain skills in order to translate knowledge into performance. It is the level of competency that allows for performance to be superior in the field in which the employees have the required skill. All managers need to possess technical, interpersonal, conceptual, diagnostic, communicational and political skills. The technical and diagnostic skills refer to the knowledge and ability of understanding the processes involved and scientifically analysing problems and opportunities. These human skills are the most important assets of any successful manager.

It is the manager's job to achieve the organizational objectives through proper utilization of its human and material resources. However, since the material resources such as equipment, capital, facilities and information can only be used by humans, the human resources are the most valuable assets of any organization. Accordingly, a manager must be highly skilled in the art of optimally utilizing the human resources. The various skills that the managers must possess are:

- Technical skills
- Human skills
- Conceptual skills
- Diagnostic skills
- Communication skills
- Political skills

Technical skills

Technical skills basically involve the use of knowledge, methods and techniques in performing a job effectively. Technical skills are specialized knowledge and expertise, which is utilized in dealing with day-to-day problems and activities. For example, engineers, accountants, computer programmers and systems analysts, all have technical skills in their areas and these skills are acquired through education and training. These skills are highly necessary at the lower level of management and as one moves to higher levels of management, the relative importance of technical skills usually diminishes. This is so because unlike the first-level supervisors, managers at higher levels have less direct contact with technical operating problems and activities at the lower levels of an organization.

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Human skills

Human skill is the ability to work with other people in a cooperative manner. It involves understanding, patience, trust and genuine involvement in interpersonal relationships. These are interpersonal skills and are necessary at all levels of management. People with good interactory human skills build trust and cooperation as they motivate and lead and thus become successful managers. This skill is gaining more importance as the workplace is becoming more and more ethnically diversified and the manager has to be aware and become adaptive to cultural differences. Furthermore, since businesses are becoming more and more multinational and global, managers are required to learn new ways of dealing with people in different countries with different cultures and value systems.

Conceptual skills

Conceptual skill is the ability to view the organization as a whole and as a total entity as well as a system comprising of various parts and subsystems integrated into a single unit. This skill is especially crucial for top-level executives who must keep the whole system under focus. They must understand the complexities of the overall organization, including how each unit of the organization contributes towards the overall success of the entire organization. This skill generally depends upon an organized thinking process which deals with the understanding of various functions of an organization, their interdependence and the relationship of the organization with the outside environment in terms of threats and opportunities.

Diagnostic skills

Diagnostic skill refers to a manager's analytical ability where a manager can logically and objectively investigate and analyse a problem or an opportunity and use scientific approaches to arrive at a feasible and optimal solution. It is important however, that a manager gets to the root cause of the problem so that the solution is real and a permanent one rather than simply a short-term or a cosmetic one. This skill overlaps with other skills because a manager may need to use technical, human, conceptual or political skills to solve the problem that has been diagnosed.

Communicational skills

Communicational skills are an important component of interpersonal skills and are basic to all other skills and these are important and necessary at all levels of management. A manager's best ideas will have little impact if they cannot be communicated effectively. Good communication is the foundation of sound management. Proper communication eliminates delays, misunderstanding, confusion, distortions and conflicts and improves coordination and control. All the four communicational skills, namely writing, reading, listening and non-verbal gestures are important ingredients of successful leadership.

CHECK YOUR PROGRESS

8. What are the characteristics of good corporate governance?
9. What skills must a manager possess?

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Political skills

Political skill can be described as the ability to get your own way without seeming to be selfish or self-oriented. It is the ability to get your share of power and authority and use it without the fear of losing it. It is the most complex of skills in the sense that it is required to establish the right connections and impressing the right people and then skillfully using these connections to your own advantage. Political skill is most important at the middle management level because middle managers always aspire to reach the top levels of management and right connections help in such aspirations.

3.5.8 Leadership Strategies in Corporate Governance

Leadership strategies have a very important role to play in corporate governance. A manager of an organization must be a good leader and must possess very good leadership strategies to effectively lead the group of employees in order to achieve the goals and objectives. Leadership is very crucial for the success of an organization. Leadership is an integral part of organizations and plays a vital role in organizational operations. It provides direction, guidance and confidence to the employees and helps in the attainment of goals in a much easier way. In industrial organizations, managers play the role of a leader and activate the employees in order to make them work.

Need for leadership strategies

The various reasons why the organization needs leadership strategies are:

- Leadership is needed for influencing the behaviour of employees of an organization.
- It is needed to coordinate the activities of the employees of an organization.
- It is needed to attain the tasks that are assigned to the employees be giving them instructions.
- It is needed to provide the employees a vision for the future.
- Leadership is needed for encouraging the employees.
- A leader is a friend to the employees. Only a leader can recognize the talents of individuals, and help them realize their dreams.
- It is only possible for a leader to unite the employees as a team.
- Only a good leader can build up a high morale within a team.
- A leader is required to help the team focus on a common goal or mission.

According to Koontz and O'Donnell, 'The leadership is an art of influencing people so that they will strive willingly and enthusiastically towards the achievement of group goals'. It emphasizes the fact that the leaders help people to understand the objectives of an organization. Thus, leadership is an endless process of influencing people to willingly and enthusiastically strive towards the achievement of the organizational goals. The leader of an organization must possess the following qualities:

- ***Smartness**:* A leader should be smart enough to solve the problems of employees.

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- ***Knowledge of business***: A leader should have a good grasp of business, and the organizational goals should be clear in his mind.
- ***Decisiveness***: A leader should be a good listener, that is, he should take a decision after taking the opinion of employees.
- ***Willingness to admit mistakes***: A leader should accept all the mistakes and learn from them in order to maintain his dignity.
- ***Innovative***: A leader should be innovative in order to meet various environmental changes.

Emerging perspectives on leadership in organizations

There are two new perspectives that have attracted attention in organizations. These are the concepts of substitutes for leadership and transformational leadership.

Substitutes for leadership

The behaviour of a leader must be appropriate for different situations. This does not include situations where leadership is not required. This concept recognizes situations where the characteristics of the subordinates, the task and the organization replace the leaders' behaviour. For example, when a patient is admitted to an emergency room in a hospital, nurses, doctors and attendants act immediately without waiting for directive or supportive behaviour of leaders in an emergency ward.

Numerous traits of the subordinates may alter or replace the leader's behaviour. For instance, employees who are able and also have relevant experiences do not require to be instructed on what to do. The features of the job that may substitute leadership are intrinsic satisfaction and the availability of feedback. For instance, the subordinate may not need direction when the task is uncomplicated and routine. However, he may require or want support when the task is challenging.

Organizational traits that may substitute leadership are group cohesion, formalization, a rigid reward structure and inflexibility. Thus, for example, leadership may not be required when policies are official and inflexible.

Transformational leadership

There are various new concepts of leadership that are used by the organization, such as charismatic leadership, inspirational leadership, symbolic leadership and transformational leadership. These new concepts of the leadership transmit a sense of mission, increase learning experiences and inspire new ways of thinking among the leader.

Charisma is a form of interpersonal attraction. Charismatic people attract followers and this type of leader has great power over his or her followers. Charismatic leaders are self-confident and can influence others. The followers of a charismatic leader identify with the leader's beliefs, accept, trust and obey the leader without questioning him and thereby contribute toward the success of the organizational goals.

3.5.9 Developments in Corporate Governance

The purpose for which an organization is being established has to be defined. An organization must not just state what they can offer to the customers. but they

CHECK YOUR PROGRESS

10. What qualities should the leader of an organization possess?

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must also state what will be required by customers in the future and the manner in which these demands can be fulfilled.

The CEO must possess an ability to clearly identify the stakeholders. The managers, workers, suppliers and the government all form the stakeholders of an organization. A CEO must clearly define the importance of all these stakeholders. The organization must maintain a very good relationship with the stakeholders. The relationship between the organization and the stakeholders is very critical for the success of an organization. Later, the organization must also maintain an effective relationship with the suppliers. Suppliers are the persons who supply raw materials in an organization. A good relationship with the suppliers will ensure the timely supply of the raw materials in an organization. An organization must also make timely payments to the suppliers in order to maintain a regular supply of raw materials in an organization.

In order to maintain an effective business strategy, an organization must have a full understanding of the vision, mission, values and responsibilities towards the shareholders. During the event of any crisis, an organization's relationship with the stakeholders and the suppliers will go a long way in protecting the organization during the time of crisis.

In the future, an organization must have a clear understanding with its stakeholders. An organization must involve the stakeholders in their decision process. The managers must be accountable for the decisions that they take in an organization. If the manager takes any decision that is not beneficial for the organization in the long run, then the manager must be held liable for any losses that the organization suffers. An organization must make a very purposeful accountability plan which must be linked with the performance of the managers. The role and responsibility of the employees must be clearly defined by the organization. The various changes that will take place in the 21st century are:

Balance accountability and enterprise

The CEO of an organization must show results in a very short period of time. A CEO must perform the tasks in a very well-planned manner. If any act of the CEO results in losses for an organization, then the CEO is held accountable for his actions and this may ultimately result in his ouster from the organization. There is a certain element of risk associated with taking decisions, which could either bring a lot of profits or losses. A good CEO is one that has a very good knowledge of the risk factor and planning in an organization. A CEO can take more accurate decisions if he has a complete knowledge of his competitive strengths and weaknesses.

Search for competitive knowledge

The CEO of an organization must continuously try to gain and maintain the competitive advantage of an organization. A CEO tries to gain competitive advantage with the help of the 4Ps, which are product, price, placement and promotion. A CEO must always be quick in taking the decisions regarding the need of the market. However, competitive advantage could result in losses for an organization. If an organization gains competitive advantage in the market by lowering the prices of products, then it may lead to a belief among the customers that the price reduction is due to poor quality of the product. This may lead to a decrease in the sales of the products of an organization, which, in turn, affects its profit.

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Accountable entrepreneurs and directors

One of the main tasks of an entrepreneur is to provide quality goods to the customers at the right price with the help of proper distribution channel. A right decision taken by the entrepreneurs goes a long way in providing an impetus to the employees for performing to the best of their abilities. The entire division of organization must work in accordance with each other to achieve the goals and objectives of the organization. The directors and entrepreneurs of an organization must be well-accountable for their actions as the decisions taken by them could either make or destroy the organization.

Corporate governance and stakeholders

Corporations are always concerned about the interest of the stakeholders of the corporation. Stakeholders also take care about social causes and the commercial value of society in relation to different interest areas of the stakeholders. The success of different corporations is dependant on the operations of the organizations, which are performed to provide profit to the stakeholders of the corporation. Stakeholders of a corporation are of four types:

- ***Primary social stakeholder***: These are those stakeholders who have direct relations with the corporation. The presence of these stakeholders in the corporation can affect the progress of the corporation.
- ***Primary non-social stakeholder***: These are also directly related to the corporation, but they are never present in the corporation as primary social stakeholders.
- ***Secondary social stakeholder***: These are those stakeholders who are not directly related to the corporation but changes in these stakeholders can affect the corporation.
- **Secondary non-social stakeholder**: These are those stakeholders who are not related to the corporation and can rarely affect the corporation.

Figure 3.4 shows the different stakeholders of a corporation.

Primary social stakeholder	**Primary non-social stakeholder**
Customers Suppliers Investors Managers and employees Local communities Business Partners Global citizen	Natural environment Future generation
Secondary social stakeholder	**Secondary non-social stakeholder**
Government Society Unions Media and communicators Trade bodies Competitors	Environmental pressure group Animal welfare pressure group

Figure 3.3: *Stakeholders of a Corporation*

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3.5.10 Corporate Governance Models

Corporate governance models are required to make an outline of the corporate governance structure of a corporation. Corporate governance structure is determined by various factors of the corporation. These factors are the rights and responsibilities of different members of the corporation, internal factors such as the working environment and the policies of corporation and external factors such as the capital market of the country.

There are several members involved in a corporation, who have different rights and responsibility. A fluent communication between these members is required for a healthy environment in the corporation. Different models for corporate governance are required to provide fluent communication between all members of the corporation. Models for corporate governance arrange all the important members of the corporation in a well-structured manner that follows various government policies related to the capital market of the country. There are two different models used to govern a corporation. These are as follows:

- Outsider model
- Insider model

Each model for corporate governance has different participants, corporate actions, regulatory framework and disclosure requirement. Participants are those members of corporation who play an important role in the corporation. Stakeholders, shareholders, CEOs, related industrial groups and management of the corporation are examples of different participants of the corporate models. Corporate actions are used to describe essential actions, which are taken by different members of the corporation. Electing directors for the board of corporation and the appointment of auditors of the corporation are examples of corporate actions. Disclosure requirements determine necessity, such as interaction between different participants of the corporation that is used to perform various corporate actions of the model. Figure 3.4 shows the different models for corporate governance.

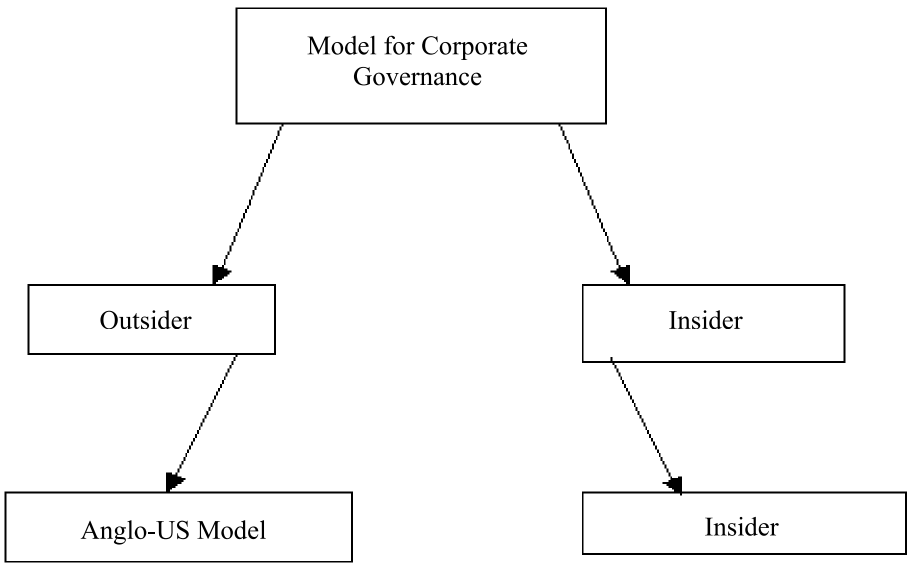

Figure 3.4: *Models for Corporate Governance*

Outsider model

European countries, such as England, as well as America, generally follow the outsider model. The outsider model is also known as shareholder model because in this model, ownership of the corporation is divided among a number of shareholders of the corporation. Thus, the financial section of the corporation is divided among different shareholders of the corporation. The corporate bodies that use the outsider model of corporate governance mostly have a good financial position in the stock market. Different banks help the clients of a corporation that uses the outsider model of corporate governance to obtain short-term finance. The outsider model has the following features:

- A priority to market regulation.
- There is a transitory interest in the firm on part of the owners.
- The absence of close relationships between shareholders and management.
- The primacy of shareholder rights over those of other industrial groups.

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Insider model

Most countries except European countries follow the insider model. This model is also known as the stakeholder model because those people who have long-term relationship with the corporation hold the entire control and ownership of the corporate body. Stakeholders of the corporation are examples of such people. Stakeholders of a corporation can be categorized as follows:

- Employees of the corporation
- Customers of the corporation
- Management
- Creditors
- Suppliers
- Local communities

The financial section of the corporation that uses the insider model is not distributed among different outsiders such as the shareholders of the corporation. In this model, the bank is an important part of the corporation that monitors clients of the corporation. The insider model has the following advantages and disadvantages:

- Priority is given to stakeholders' control.
- The firm owners show a long lasting interest in the company.
- They, many a times, hold positions in senior managerial positions or on the board of directors.
- The relationships between management and shareholders are close and stable.
- The formal rights of employees exist so that the key managerial decisions can be influenced.
- There is hardly any market for corporate control.

Insider model in eurasian countries

In most countries, such as the Eurasian countries, which constitute all European countries except England and America, and most Asian countries, the insider model is used for corporate governance. The following are the various aspects related to the insider model for corporate governance in Eurasian countries:

- The mass privatization with favourable conditions for employees in Eurasian countries has created prerequisites for the insider model of corporate governance.
- The Russian tendency that the employees' shares pass to other holders is also present in Eurasian countries but not so sharp.
- For some countries, there is high concentration of the shares' capital at the management.
- Nevertheless, employees continue to play an important role as shareholders in Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Ukraine and Uzbekistan.

International private initiatives in corporate governance

The role of employees in corporate governance has an important place in widespread corporate governance guidelines and codes of conduct as, for example, in Corporate Governance Forum Principles (1998), Bosh Report, General Motors Board Guidelines, Dey Report and others (Holly J. Gregory, international comparison of board 'Best practices' in developed markets, 1999).

3.5.11 Corporate Governance Structure

The corporate governance structure of a corporation is affected by several factors such as the country to which a corporation is related, responsibilities and roles of different participants of the corporation and the position of the corporation in the capital market. In other words, the corporate governance structure of any corporation varies according to a specific factor, which is the country to which the corporation is related. There are two different models used to govern different corporations according to their corresponding countries. These are as follows:

- The Anglo-US model
- The Japanese model

The Anglo-US model

The Anglo-US model is an outsider model used for corporate governance. This model is influenced by share ownership of an individual or an outsider. The Anglo-US model is a well-maintained framework, which is used to represent different roles and responsibilities of different participants of a corporation, such as management, shareholders and directors. This model provides an easy way of communication between different participants, because this model maintains good relations between different participants of the corporation. This model is used by those countries, which have the largest capital market in the world. USA and UK are good examples of these countries. Most of the corporations of these countries use equity financing for increasing their capital values.

The Anglo-US model also maintains a causal relationship between different factors of a corporation such as equity financing, capital market size of corporation and corporate governance structure. In this model, shareholders play the most important role in maintaining capital market and corporate governance of the corporation among all other participants of corporation. Figure 3.5 shows the different participants of the Anglo-US model used for corporate governance.

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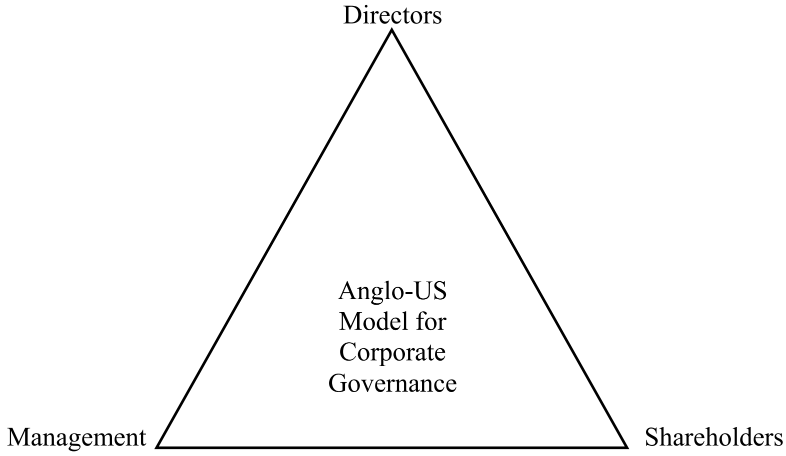

Figure 3.5: *Different Participants of Anglo-US Model*

According to the Anglo-US model, ownership and control of the corporation is distributed among different shareholders of the corporation. Distribution of ownership and control among different outsiders helps the corporation in maintaining a strong capital market, because outsiders contribute their efforts and capital to make a strong position of the corporation in the market. A strong position of a corporation in the capital market increases the profit of the shareholder. The cost of distributing ownership and control among different outsiders is known as agency cost.

In the early days of the use of the Anglo-US model, corporations in the US and UK had only two types of participants—individual shareholder and institutional shareholders. After some time, the board of directors of the corporations was also involved in the list of participants of the Anglo-US model. The board of directors consisted of many insiders and outsiders. Insiders refer to those people who have a strong relationship with the corporation, such as employee, manager and stakeholder. Outsiders refer to those people, who are not directly connected with the corporation. Shareholders and investors are examples of outsiders of corporation.

Outsiders such as individual and institutional investors observe many running factors of corporations to know about the trends of corporation and to represent their interest in corporations.

Observation is necessary to obtain more information about the corporation so that they never face the problem of lack of information which is one of the most common problem that outsiders of a corporation face. Lack of information is also a limitation for outsiders because of which they never provide their effective oversight to the corporation.

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Corporations using the Anglo-US model for corporate governance attract many outsiders due to the following reasons:

- Attracting pattern of stock ownership
- Increasing importance of institutional investors among all participants of corporation
- Importance of outsiders in the Anglo-US model's voting behaviour
- Better proposal of private corporations such as Committee on the Financial Aspects of Corporate Governance and Shareholder Corporation

Necessity of the Anglo-US Model

When the board of directors were involved in the list of participants of the Anglo-US model, the entire power of ownership and control of corporation was moved to the hands of Chief Executive Officer (CEO). The person controlling the power can cause the occurrence of negative factors. These factors are as follows:

- All decisions related to corporation is dependent on one person.
- Sometimes, a group of insiders can control the corporation.
- In many cases, insiders or CEOs are always concerned about their own profit.

A lot of outsiders started becoming involved as participants of corporations because of the above reasons. Many factors contribute to increasing the interest of corporate governance with the involvement of outsiders. These factors are as follows:

- Provision of new government regulations
- More involvement of institutional investors
- Introduction of takeover activity
- More competitiveness with Asian countries's corporation

Regular Framework in the Anglo-US Model

Anglo-US model provides a well-maintained relationship between all the participants of the corporation. In America, a centralized agency, Securities and Exchange Commission (SEC) is used to regulate communication between all participants of corporation involved in the Anglo-US model.

The size of the capital market and communication system, of corporation affects the framework of Anglo-US model. Many laws related to funds and finance of a country also regulate the corporate governance. In England, framework of corporate governance is established according to its parliamentary rules, which is established by private or self-regulatory firms such as security and investment board. The security and investment board maintains the securities market of the corporation.

Disclosure requirement

In the Anglo-US model, corporations require the distribution of information among all participants of the model. Information can be released by an annual report, which contains the following information:

- Entire financial data of the corporation
- Breakdown of capital structure of corporation

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- Name, occupation, corporate relationship of every member involved in the board of directors as a member of the Anglo-US model
- The compensation paid to the upper management and the CEOs of the corporation
- List of all shareholders, who have more than 5 per cent of corporation shares
- Name of the auditors of the corporation
- All the factors that are used to restructure any part of the corporation

Shareholders are also permitted to submit their proposals in the report represented in the Anglo-US model. These proposals are known as shareholder proposals. Shareholder proposals include information about those activities which are related to the corporation's progress.

Note: *All the corporations in UK and other countries use the semi-annual report.*

Corporate actions

Corporate actions in the Anglo-US model require the approval of shareholders. The shareholders, who have more than 10 per cent of the total share of the corporation, have permission to assemble an extraordinary general meeting (EGM) for approving different corporate actions. These actions are of two types—routine actions and non-routine actions. Routine actions include election of directors and appointment of auditors of the corporation. Non-routine actions involve the establishment of stock option plans mergers and takeovers and the restructuring of any part of corporation, if required.

The Japanese model

In the Japanese model, stakeholders of the corporation hold ownership and control of the corporation. The main bank system provides most of the finance for the company requirements. In other words, it is the largest creditor of the corporation. It provides cross shareholding arrangement to the corporation that make the bank one of the important shareholders of the corporation. The main bank system is responsible for monitoring investment decisions and various clients of the corporation. It is also concerned with the running progress of the corporation. It provides financial help to the corporation. The main bank system is responsible for handling the client of the corporation. It provides the following services to the clients for handling clients of the corporation:

- Enabling long-term investment of clients
- Securing lender of the corporation
- Providing stability to the shareholders of the corporation
- Providing solution to the problem of irregularity of information
- Managing the financial position by gathering rents from excessive deposits

Japanese corporations mainly use the Japanese model, where equity financing is one of the most important financing factor of the corporation. The stakeholders of the corporation help in maintaining good relationships between the main bank system and the corporation. This model requires a legal and well-maintained framework to promote industrial groups. Industrial groups are related with the corporation using cross share holding of equity and trading relationship. Industrial groups are known as keiretsu in Japan.

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The Japanese model is mainly used by Japanese corporations, where equity financing is one of the most important financing factor of the corporation. Stakeholders of corporation are also one of the most important factors of Japanese corporations. They play an important role in the corporation and its entire system. In Japanese corporations, outsiders do not play as important a role as in Anglo-US model, because outsiders never take more interest in the corporation's profits and loss.

Participants of Japanese model

The Japanese model of corporate governance has many participants, which are as follows:

- The main bank system
- Keiretsu
- Management
- The government of the country
- Shareholders
- Independent directors

Main bank system

The main bank system is one of the most important participants of the corporation. It is concerned with the financial position of the corporation. It also provides financial help to the corporation if required to maintain a good position in capital market of the country. The main bank system is responsible for handling the various clients of the corporation and also helps corporations in providing their customers with services related to loans, equity issues, bond issues, settlement account and consultancy services. It is one of the major shareholders of the corporation.

Keiretsu

Keiretsu refers to those industrial groups that are related to the corporation in terms of handling different financial transactions of the corporation. It also plays an important role in the Japanese model of corporate governance. Keiretsu is responsible for handling debt and equity transactions of the corporation, trading of products of the corporation and informal business contacts.

Management

The management of the corporation is responsible for managing communication between the insiders and the stakeholders of the corporation. Managing communication between different insiders is an important task in any model. Thus, the management of the corporation is also an important participant of the corporation, and it uses the Japanese or insider model of corporate governance.

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The government of the country

The government of the country in which the corporation is established also affects the model of corporate governance by introducing different policies related to the corporation. For example, in the 1930s, the Government of Japan introduced a policy, according to which every corporation has to show official and unofficial representation on its corporate board when the corporation faces financial problems.

Shareholders

Outside shareholders are not very important participants in the Japanese model. There is a very small number of shareholders in corporations, which is the reason behind the less significance of these participants in the Japanese model.

Independent directors

Independent directors refer to the chief executive officer (CEO) of the corporation. In Anglo-US model of corporate governance, CEOs of the corporation play an important role, but in the Japanese model, CEOs do not play such important role as in the Anglo-US model. These CEOs represent the outside stakeholder of the corporation who is only responsible for getting profits.

The main bank system, keiretsu, the management and the government are important participants in the Japanese model of corporate governance. Shareholders and independent stakeholders are two other participants that do not have not so much importance as the other four participants. Figure 3.6 shows different participants of the Japanese model.

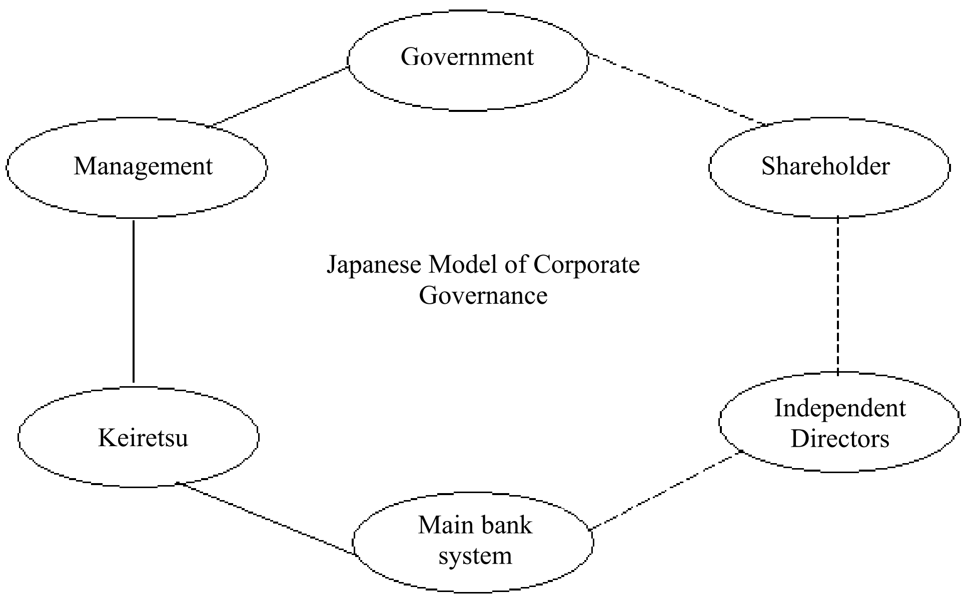

Figure 3.6: *Participants in the Japanese Model*

In the above figure, the dashed lines show the less significant participants of the Japanese model. Shareholders and independent directors are less significant participants of Japanese model of corporate governance, because these participants are in very few numbers and are only interested in their share of the corporate profit.

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Solid lines show the important participants of the Japanese model of corporate governance. Government policies, management processes such as communication management, industrial groups, which help corporations in the distribution of products and other services that are known as keiretsu, and the main bank system are the most important participants of the Japanese model.

Composition of the board of directors

The board of directors in the Japanese model contains fifty members that include executive manager of corporation, heads of different departments of the corporation and administration of the corporation. The executive manager, heads of departments and administration of the corporation are directly connected to the corporation. In the other words, all the members of board of directors are insiders of the corporation.

The main bank system and keiretsu of the corporation can also add new members in the board of directors. For example, if a corporation takes more time to get the required profit than expected, then other participants such as keiretsu and the main bank system of the Japanese model appoint their own member in the board of directors. Some corporation also include government bureaucrats in the board of directors, because they help corporations in managing the financial section of the corporation.

Regulatory framework

Japanese government ministries frequently develop industrial policies according to the role of Japanese corporations in the international market. The Ministry of Finance and the Ministry of International Trade and Industry are also responsible for formatting different industrial policies. Industrial policies are changed due to the following reasons:

- Japanese corporations are becoming more and more globalized day by day, which makes Japanese corporations more dependent on the domestic market of other countries.
- Most of the Japanese corporations have become partially liberalized in the international capital market and opening to global standards.

Regulatory framework of Japanese model has developed after World War II. Government agencies of Japan provide little effective, independent regulation of the Japanese securities industry.

Disclosure requirements

Disclosure requirements of the Japanese model are somewhat similar to the Anglo-US model of corporate governance. In the Anglo-US model, an annual report, which contains information about different factors such as financial performance of the corporation and members of the board of directors of the corporation, is required. The main difference between the Japanese and the Anglo-US models is that in the Anglo-US model, the annual report is represented to the board of directors while in the Japanese model, semi-annual information is provided in the reports represented to the board of directors. This report includes information about financial data of corporation, name and information about top ten shareholders of the corporation.

Corporate Action

In the Japanese model, corporate actions are divided into routine corporate actions and non-routine corporate actions. Routine corporate actions include the following actions:

- Paying dividends and allocation of reserves
- Election of directors
- Appointment of auditors
- Authorization of the capital of the corporation to the bank
- Management of the required changes of the corporation
- Payment of the retirement bonuses to the directors and auditors
- Providing compensation to the directors and auditors

Note: *Non-routine corporate action is similar to the Anglo-US model of corporate governance.*

Interaction among different participants

In the Japanese model of corporate governance, interaction among different participants produces a strong relationship between each other. Interaction is one of the basic characteristics of the Japanese model. In the Japanese model, good interaction is required because the main participants of the Japanese model are the insiders of the corporation, This requires fluent communication for the distribution of knowledge about each factor of the corporation. Various reports and annual general meetings (AGM) are used to provide good interaction between different participants in the Japanese model.

3.5.12 Overview of Various Codes of Corporate Governance

There are various codes of corporate governance that the organizations have to implement. The Cadbury code originated in the United Kingdom and it led to the development of the various other codes. The Kumaramanglam code originated in India as a result of the committee that was headed by the Shri Kumaramanglam at the Securities and Exchange Board of India (SEBI). However, the codes are only guidelines, which the organizations must follow to achieve the goals and objectives of the organization. For the corporate governance code to have real meaning, it must first focus on the listed organizations. The organizations that are listed are largely financed by the public money such as equity and debt securities. There are three aspects of codes of the corporate governance. These are the following:

- There is a set structure of corporate governance available worldwide. Therefore, a code of corporate governance cannot be designed for an individual's own purpose.
- Better corporate practices can no longer afford be ignored by Indian companies and financial institutions.
- Corporate governance is far beyond the company law. It is difficult to legislate in detail the quantity, quality and the length to which the board of directors exercise their responsibilities towards the shareholders.

The Cadbury Code [1]

In the post Enron era, much regulatory attention has been given to non-executive directors (NEDs) and their role in contemporary corporate governance. The Higgs Review (2003) in the UK suggested the potentially important role or non-executive directors in improving corporate governance. As part of the firms' board, non-executive directors participate in monitoring and controlling the executive layer of the firm. The UK regulatory scene has sought to encourage good corporate behaviour through a 'comply or explain' approach with fines and imprisonment as a last resort. In contrast, the US with its Sarbanes Oxley legislation has not actively promoted the role of non-executive directors. Instead the US has used the threat of fines and imprisonment to deter undesirable corporate behaviour. For example, the US approach can be seen in the 25-year prison sentence given in July 2005 to Bernard Ebbers, former CEO at WorldCom, and the 24-year sentence given in October 2006 to Jeffrey Skilling, former CEO at Enron.

According to the UK approach, to serve as an effective counterweight to the executive layer in the board, non-executive directors are expected to be independent from the firm they take part in directing. Therefore, the role of non-executive directors follows a risk-regulatory rationale. By serving as a counterweight to the top executive part of firms, non-executive directors are indented to limit the risk of excessive power concentrating in the hands of the chief executive officer and senior executive board members. Therefore, in spite of the crucial importance attributed to non-executive directors' independence, as it evolved in the last decade, is lacking, misguided and introduces a considerable source of risk to the governance of large corporation and, through a systemic effect, to the entire economy.

There are inherent problems regarding the regulatory requirements from boards of directors. In the UK, in reaction to various corporate scandals in the last two decades, a chain of regulatory documents were published, starting at the Cadbury Report, followed by the Greenbury Committee, the Hampel Committee and culminating in the first version of The Combined Code in 1998, each stressing more forcefully the importance of appointing independent non-executive directors for transparent and efficient corporate governance.

The evolution of the regulatory definitions regarding the independence of NEDs shows a gradual crystallization of two related concepts such as the negative probabilistic concept and the negative bilateral concept. Practices following the negative bilateral concept assign an independent status to a director according to his/her lack of connections with a specific firm. In contract, the negative probabilistic concept regards a director as independent according to their lack of connection with certain categories or groups in the general population.

These two concepts, which together dominate the British regulatory discourse about non-executive directors, contain several problematic characteristics that may bring about systemic risks. First, the concepts do not define positively what counts as directors' independence, but only provide a 'by-default' deducible definition. Hence, the regulators cannot assess to what extent firms are interdependent and to what degree their interlocking connections may affect their decision-making. Second, the existing regulatory concepts create a situation in

[1] http://www.essex.ac.uk/afm/Publications/CARR_magazine_paper_draft_061030.pdf

which the recruitment of non-executive directors becomes a utility-maximization exercise (in effect, a zero-sum game). Therefore, in so doing, the regulation effectively channels firms to circumvent the regulatory recommendations.

The Negative Bilateral Concept[2]

The Cadbury Report, published in 1992, was the first attempt to focus on non-executive directors as an important mechanism for improving governance in UK quoted companies. The preface to the report of the Cadbury Committee referred to 'the continuing concern about standards of financial reporting and accountability, heightened by Bank of Credit and Commerce International (BCCI), Maxwell and the controversy over directors' pay which has kept corporate governance in the public eye' (Cadbury Report, 1992: 9). The Cadbury Report recommended that quoted company boards should each have a minimum of three non-executive directors. It was recommended that a majority of the non-executive directors should be independent, that is they should be independent of the management and free from any business or other relationship which could materially interfere with the exercise of their independent judgment. (Cadbury Report, 1992: 22).

The Cadbury Report signifies the beginning of the bilateral negative definition for non-executive directors' independence: the less connections there are between the director and the firm, the more independent the director is deemed to be. Three years after the Cadbury report, the Greenbury Committee was formed following widespread public concern over what were seen as excessive amounts of remuneration paid to directors of quoted companies and newly privatized companies. The Greenbury Committee recommended that the remuneration committee should consist exclusively of non-executive directors. These non-executive directors should have no personal financial interest, other then as shareholders, in the committee's decisions. Also, there should be no cross-directorships with the Executive Directors, which could be thought to offer scope for mutual agreements to bid up each others remuneration' (Greenbury Report, 1995: 22, 23).

Also in 1995, the Hampel Committee published a report in which it reviewed the implementation of the findings of the Cadbury and Greenbury Committees. The Hampel Committee recommended that 'boards should disclose in the annual report which of the directors are considered to be independent and be prepared to justify their view if challenge'. Principles of Good Governance and Code of Best Practice were published by the London Stock Exchange in 1998. The recommendation to disclose the independence status of the directors and the backing of that recommendation by the London Stock Exchange signified a further strengthening of the bilateral concept: the corporate discourse that interprets the board's independence was no longer hidden, but was placed in the public domain.

The Negative Probabilistic Concept

In 1998, following a string of financial scandals including those of Enron and WorldCom, Derek Higgs had been commissioned by the UK government to review the role and effectiveness of non-executive directors. Public confidence in

[2] http://www.essex.ac.uk/afm/Publications/CARR_magazine_paper_draft_061030.pdf

non-executive directors had been eroded, for example, by reports that a third of non-executive directors are recruited through personal contacts (the old network) and that Lord Wajeham, a former UK government cabinet minister, sat on the boards of sixteen companies. For example, the report stated that the nomination committee should 'consider candidates from a wide range of backgrounds and look beyond the 'usual suspects'. The Higgs Review also led to the Department of Trade and Industry commissioning a report on the recruitment and development of non-executive directors. This report (The Tyson Report, 2003) explicitly recommends increased diversity in board membership, particularly with regard to female participation.

In addition, Higgs recommended that the nomination committee should consist of majority of independent non-executive directors and should be chaired by an independent non-executive director. The nomination committee should lead the process for board appointments and make recommendations to the board. These recommendations (with some minor changes) were incorporated in a revised (2003) version of the Combined Code. Following a review by the Financial Reporting Council in 2005, a few minor changes were made to the latest version of the Combined Code, published in 2006.

In addition, one must stress on the importance of directors' independence to proper corporate governance The Combined Code also states that on the boards of all FTSE 350 companies, 'at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent'. (A.3.2). In their decisions, the Higgs Committee and the Combined Code entrenched the independence according to the negative probabilistic approach more deeply by focusing on nomination of directors. Decisions made by a nomination committee would be independent of the board as long as and to the extent that its members are themselves independent. Hence, by recommending that nomination committees will be composed of non-executive directors, the committee introduced a structural-recursive element that, in effect, distanced the board from a position of responsibility and accountability. By calling for a more diverse background from which directors are appointed, the Combined Code has tried to offer a potential remedy to the 'negative' definition approach and its problems. The implicit assumption here is that if NEDs come from outside the social networks of the existing directors, it is more likely that they would be independent. The organizational tools that are expected to ensure a wide diversity of appointees are set procedures that firms must follow prior to appointments.

The presentation of the probabilistic approach may seem like a solution but in fact it simply moves the 'negativity' problem to a different location. By demanding firms to appoint non-executive directors from 'diverse backgrounds' the Combined Code actually asks the firms to appoint non-executive directors from backgrounds that are different from those from which NEDs usually came. Hence, the Combined Code still does not provide a positive definition about directors' independence, but only a deducible, 'by-default' definition. Assuming that there is a correlation between expertise and vicinity to the firm, simply asking firms to diversify their appointments is not likely to diminish the causes for the knowledge versus connection optimization process that firms currently perform.

The developments reviewed above reveal that although non-executive directors' independence is regarded as an important regulatory resource and as a vital attribute of corporate governance, the two negative definitions of independence, the bilateral and the probabilistic, leave the question of defining positively the independent directors unanswered. This fact creates a regulatory loophole that allows British companies to appoint a wide variety of people as directors without providing any positive benchmarks against which the appointments' independence could be assessed. Furthermore, the definitions create an implicit, but potentially risky, trade-off between independence and expertise. The negative definitions state that a non-executive director would be deemed independent if he or she is not connected to the firm. These definitions are likely to bring about a mode of operation in which the firms would link at the appointment of non-executive directors as an optimization exercise between independence of the appointed director and his/her relevant knowledge and expertise. Thus, under these regulatory definitions, it is likely that companies would try to appoint non-executive directors that are as expert as possible and satisfy the minimal independence criteria.

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To address the inherent problems of the non-executive directors' independence concept, an individual needs to think about an alternative concept to that of independence. Instead of defining people and boards of directors according to a bilateral binary scheme (where they could either be independent or non-independent and in relation to only a single organization or person) An individual should consider a decision that would assess the degree of connectedness of each of the non-executive directors in relation to the entire network of connections. This alternative conceptualization brings with it a host of regulatory challenges. The fundamental conceptual difference between directors' independence and directors' connectedness lies in the scope of analysis. To determine the degree of independence of a director vis-à-vis a board, it is necessary to examine and assess the strength and efficacy of the connections between the individual director and a specific company.

In contrast, to measure the director's connectedness, one would need to trace the network of connections of which the board member is part and then to establish how important is the role of the specific board member in maintaining the structure of connections among other members, and through them, among companies. What are the advantages that this concept can bring to corporate regulation. The interconnected view of corporate boards will allow us to place independence in wider perspective. That is, directors may not be associated with a company in a direct business respects (not sure how this should be phrased of whose board they are members). However, this does not show us the complete picture. An interlocking position of board members makes them crucial in relaying information among the economic organizations. Therefore, studying the inter-board network as a predominantly informational arena allows us to provide a more comprehensive interpretation to the nature of directors' independence in it.[3]

Kumarmangalam Birla Committee Report

The report of the Kumaramangalam Birla Committee on corporate governance states that it is almost a truism that the adequacy and the quality of corporate governance shape the growth and the future of any capital market and economy. The concept of corporate governance has been attracting public attention for quite

[3] http://www.essex.ac.uk/afm/Publications/CARR_magazine_paper_draft_061030.pdf

some time in India. The topic is no longer confined to the halls of academia and is increasingly finding acceptance for its relevance and underlying importance in industry and the capital market. Progressive firms in India have voluntarily put in place systems of good corporate governance. Internationally also, while this topic has been accepted for a long time, the financial crisis in emerging markets has led to renewed discussion and inevitably focused them on the lack of corporate as well as governmental oversight. The same applies to recent high-profile financial reporting failures even among firms in the developed economies. Focus on corporate governance and related issues is an inevitable outcome of a process, which leads firms to increasingly shift to financial markets as the pre-eminent source for capital. In the process, more and more people are recognizing that corporate governance is indispensable to defective market discipline. This growing consensus is both an enlightened and a realistic view. In an age where capital flows worldwide, just as quickly as information, a company that does not promote a culture that is strong and independent, risks its very stability and future health. As a result, the link between a company's management, directors and its financial reporting system has never been more crucial. As the boards provide stewardship of companies, they play a significant role in their efficient functioning.

- Studies of firms in India and abroad have shown that markets and investors take notice of well-managed companies, respond positively to them, and reward such companies with higher valuations. A common feature of such companies is that they have systems in place, which allow sufficient freedom to the boards and management to take decisions towards the progress of the companies and to innovate, while remaining within the framework of effective accountability. In other words, they have a system of good corporate governance.
- Strong corporate governance is thus indispensable to resilient and vibrant capital markets and is an important instrument of investor protection. It is the blood that fills the veins of transparent corporate disclosure and high-quality accounting practices. It is the muscle that moves a viable and accessible financial reporting structure. Without financial reporting premised on sound, whole numbers, capital markets will collapse upon themselves.
- Another important aspect of corporate governance relates to issues of insider trading. It is important that insiders do not use their position of knowledge and access to inside information about the company, and take unfair advantage of the resulting information asymmetry. To prevent this from happening, corporations are expected to disseminate the price-sensitive information in a timely and proper manner and also ensure that till such information is made public, insiders abstain from transacting in the securities of the company. The principle should be 'disclose or desist'. This, therefore, calls for companies to devise an internal procedure for adequate and timely disclosures, reporting requirements, confidentiality norms, code of conduct and specific rules for the conduct of its directors and employees and other insiders. For example, in many countries, there are rules for reporting or transactions by directors and other senior executives of companies, as well as for a report on their holdings, activity in their own shares and net year-to-year changes to these in the annual report. The rules also cover the dealing in the securities of their companies by their companies by the insiders, especially directors and other senior executives, during sensitive reporting seasons. However, the need for such procedures, reporting requirements and rules also goes beyond corporate to other entities in the financial markets such as stock exchanges, intermediaries, financial institutions, mutual funds and

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concerned professionals who may have access to inside information. This is being dealt with in a comprehensive manner, by a separate group appointed by SEBI, under the Chairmanship of Shri Kumaramangalam Birla.

- The issue of corporate governance involves, besides shareholders, all other stakeholders. The Committee's recommendations have looked at corporate governance from the point of view of the stakeholders and in particular that of the shareholders and investors, because they are the raison d'etre for corporate governance and also the prime constituency of SEBI. The control and reporting functions of boards, the roles of the various committees of the board, the role of management, all assume special significance when viewed from this perspective. The other way of looking at corporate governance is from the contribution that good corporate governance makes to the efficiency of a business enterprise, to the creation of wealth and to the country's economy. In a sense both these points of view are related and during the discussions at the meetings of the Committee, there was a clear convergence of both points of view.
- At the heart of the Committee's report is the set of recommendations which distinguishes the responsibilities and obligations of the boards and the management in instituting the systems for good corporate governance and emphasizes the rights of systems for good corporate governance and the rights of shareholders in demanding corporate governance. Many of the recommendations are mandatory. For reasons stated in the report, these recommendations are expected to be enforced on the listed companies for initial and continuing disclosures in a phased manner within specified dates, through the listing agreement. The companies will also be required to disclose separately in their annual reports, a report on corporate governance delineating the steps they have taken to comply with the recommendations of the Committee. This will enable shareholders to know where the companies, in which they have invested, stand with respect to specific initiatives taken to ensure robust corporate governance. The implementation will be phased. Certain categories of companies will be required to comply with the mandatory recommendations of the report during the financial year 2000–2001, but not later than 31 March 2001, and others during the financial years 2001–2002 and 2002–2003. For the non-mandatory recommendations, the Committee hopes that companies would voluntarily implement these. It has been recommended that SEBI may write to the appropriate regulatory bodies and governmental authorities to incorporate where necessary, the recommendations in their respective regulatory or control framework.
- The Committee recognized that India had in place a basic system of corporate governance and that SEBI has already taken a number of initiatives towards raising the existing standards. The Committee also recognised that the Confederation of Indian Industries had published a code entitled 'Desirable Code of Corporate Governance' and was encouraged to note that some of the forward looking companies have already reviewed or are in the process of reviewing their board structures and have also reported in their 1998–99 annual reports the extent to which they have complied with the Code. The Committee however felt that under Indian conditions a statutory rather than a voluntary code would be far more purposive and meaningful, at least in respect of essential features of corporate governance.
- The Committee, however, recognized that a system of control should not impede the ability of the companies to compete in the marketplace. The

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Committee believes that the recommendations made in this report mark an important step forward and if accepted and followed by the industry, they would raise the standards in corporate governance, strengthen the unitary board system, significantly increase its effectiveness and ultimately serve the objective of maximizing shareholder value.

The Recommendations of the Committee

This Report is the first formal and comprehensive attempt to evolve a code of corporate governance in the context of prevailing conditions of governance in Indian companies, as well as the state of capital markets. While making the recommendations, the Committee has been mindful that any code of corporate governance must be dynamic, evolving and should change with changing contexts and times. It would, therefore, be necessary that this code also be reviewed from time to time, keeping pace with the changing expectations of the investors, shareholders, and other stakeholders and with increasing sophistication achieved in capital markets.

Source: http://web.sebi.gov.in/commreport/corpgov.html

3.5.13 Objectives of Corporate Governance[4]

There are various objectives of corporate governance. These are:

- Corporate governance has several claimants such as shareholders and other stakeholders which include suppliers, customers, creditors, the bankers, the employees of the company, the government and the society at large. This Report on Corporate Governance has been prepared by the Committee for SEBI, keeping in view primarily the interests of a particular class of stakeholders, namely the shareholders, who together with the investors form the principal constituency of SEBI while not ignoring the needs of other stakeholders.
- The Committee, therefore, agreed that the fundamental objective of corporate governance is the 'enhancement of shareholder value, keeping in view the interests of other stakeholders'. This definition harmonizes the need for a company to strike a balance at all times between the need to enhance shareholders' wealth, while not in any way being detrimental to the interests of the other stakeholders in the company.
- In the opinion of the Committee, the imperative for corporate governance lies not merely in drafting a code of corporate governance, but in practising it. Even now, some companies are following exemplary practices, without the existences of formal guidelines on this subject. Structures and rules are important alone but 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.
- It follows that the real onus of achieving the desired level of corporate governance lies in the proactive initiatives taken by the companies themselves and not in the external measures such as breadth and depth of

[4] http://business.gov.in/corporate_governance/kumarmangalam.php

a code of stringency of enforcement of norms. The extent of discipline, transparency and fairness, and the willingness shown by the companies themselves in implementing the code, will be the crucial factor in achieving the desired confidence of shareholders and other stakeholders and fulfilling the goals of the company.

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Narayana Murthy Committee Code[5]

The Narayana Murthy Panel Report on Corporate Governance

The whistle blower policy recommended in the recent report of SEBI's committee on corporate governance and Clause 49 of the Listing Agreement, which was headed by Mr N.R. Narayana Murthy, Chairman and chief mentor of Infosysis Technologies, seems to have evoked the sharpest response from veteran company secretaries, who have studied the key suggestions in detail.

In fact, judging by what they have to say, it is apparent that this particular recommendation, which is intended to curb unethical and improper practices in corporate, is being singled out by company law experts as simply impractical.

What is the 'whistle blower' policy? It is an internal policy on the access to audit committees. What is the committee's recommendation? Personnel who come to know about unethical or improper practices, which may not necessarily be a violation of law, should be able to approach the company's audit committee 'without necessarily informing their supervisors'.

The committee wants corporations to take steps to see that this right of access is communicated to all employees through internal circulars. Further, a company's employment and personnel policy should provide a mechanism to protect whistle blowers from 'unfair termination and other unfair, prejudicial employment practices'.

Senior company secretaries that spoke to *Business Line* said that this recommendation, if implemented, would be instrumental in breeding indiscipline as the audit committee would most likely be flooded with frivolous complaints and minor issues. Many complaints might go by their personal likes and dislikes and thus the possibility of the right of access to the audit committee being misused would always be there.

They noted that the committee had not said anything on providing evidence in support of a complaint, disclosure of the identity of the complainant and the maximum number of complaints that an employee could make in a year.

The elimination of unethical or improper practices is the responsibility of respective corporate promoters and management, for which they have to put in place systems for efficient administration and transparent transactions. Much also depends on the environment in which corporations operate and the policies that govern their operations. A whistle blower policy cannot be a foolproof safeguard against unethical and improper practices, they contend.

The recommendation regarding composition of an audit committee has given rise to confusion. While this panel has suggested that audit committee members should be non-executive directors, the Naresh Chandra committee that preceded it

[5] http://www.thehindubusinessline.com/2003/04/08/stories/2003040802200400.htm

suggested that only independent directors should be on audit committee. The reality is that while all independent directors are non-executive directors, it is not so vice versa.

Regarding contingent liabilities, it has been suggested that management's views thereon and auditor's comments on management's views should be given in the annual report. According to senior company secretaries, there are instances where contingent liability cannot be ascertained, such as labour disputes and court cases. As the description suggests, it is all contingent upon future developments and, therefore, it cannot be proper for a management to pass a judgement about the risk involved. Ideally, a management should only give the background of a contingent liability.

The Narayana Murthy panel is for restricting the tenure of non-executive directors to three terms of three years each, running continuously. The Naresh Chandra panel said that after a nine-year term the director would not be considered independent, but surely the concerned person would be able to continue as a non-executive director.

Company secretaries make two points: If the intention is to follow the Naresh Chandra committee's suggestion, the Narayana Murthy panel's recommendation should be redrafted. Representatives of a promoter remain on the board of a company as non-independent directors. The recommendation now made rules out continuation of promoter-directors on the board beyond nine years at a stretch.

It needs to be clarified whether a partner of an audit firm or a solicitor's firm can be treated as an independent director of a company if his firm is the auditor or legal advisor of another company in the same group.

On Analysis and Media Role[6]

The Narayana Murthy committee on corporate governance also discussed reports brought out from time to time by security analysts and the media, especially the financial press. As for reports of security analysts, the committee has desired SEBI to make rules, which are:

- Disclosure of whether the company that is being written about is a client of the analyst's employer or an associate of the analyst's employer, and the nature of services rendered to such company, if any
- Disclosure of whether the analyst or the analyst's employer or an associate of the analyst's employer hold or held (in the twelve months immediately preceding the date of the report) or intend to hold any debt or equity instrument in the issuer company that is the subject matter of the report of the analyst

Regarding scrutiny of the media, particularly the financial press, it has observed the committee considered views expressed by members.

The Press Council of India has prescribed a code of conduct for the financial media. However, verifying adherence to the code is difficult. A detailed review by SEBI on the subject is desirable, keeping in mind issues such as transparency and disclosures, conflicts of interest, etc., before making any rule. SEBI should consider having a discussion with the representatives of the media, especially the financial press.

[6] http://www.thehindubusinessline.com/2003/04/08/stories/2003040802200400.htm

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Naresh Chandra Committee Code[7]

Section 2.3.8 of this Report states that the Committee would also recommend that the following mandatory recommendations in the report of the Naresh Chandra Committee, relating to corporate governance, be implemented by SEBI.

This section sets out such recommendations of the Naresh Chandra Committee that were considered by this Committee.

Disclosure of Contingent Liabilities (Section 2.5 of the Naresh Chandra Committee Report)

The Committee makes the mandatory recommendation that the management should provide a clear description in plain English of each material contingent liability and its risks, which should be accompanied by the auditor's clearly worded comments on the management's view. This section should be highlighted in the significant accounting policies and notes on accounts as well as in the auditor's report, where necessary.

This is important because investors and shareholders should obtain a clear view of a company's contingent liabilities as these may be significant risk factors that could adversely affect the company's future financial condition and results of operations.

CEO/CFO Certification (Section 2.10 of the Naresh Chandra Committee Report)[8]

The committee makes the following mandatory recommendation

For all listed companies, there should be a certification by the CEO (either the executive chairman or the Managing Director) and the CFO (whole-time finance director or other person discharging this function), which should state that, to the best of their knowledge and belief. The committee makes the following mandatory recommendations:

- They have reviewed the balance sheet and profit and loss account and all its schedules and notes on accounts, as well as the cash flow statements and the director' report.
- These statements do not contain any untrue statement or omit any material fact nor do they contain statements that might be misleading.
- These statements together present a true and fair view of the company, and are in compliance with the existing accounting standards and/or applicable laws/regulations.
- They are responsible for establishing and maintaining internal controls and have evaluated the effectiveness of internal control systems of the company; and they have also disclosed to the auditors and the Audit Committee, deficiencies in the design or operation of internal controls, if any, and what they have done or propose to do to rectify these.

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[7] http://www.acga-asia.org/public/files/India_MurthyCtee_Feb03.pdf

[8] http://www.icsi.edu/webmodules/Programmes/31NC/NEWCORPORATEGOVERNANCENORMS-NKJAIN.doc

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- They have also disclosed to the auditors as well as the Audit Committee, instances of significant fraud, if any, that involves management or employees having a significant role in the company's internal control systems.
- They have indicated to the auditors, the audit committee and in the notes on accounts, whether or not there were significant changes in internal control and/or of accounting policies during the year.[9]

3.5.14 Risk Management in a Corporation

The management of a corporation is responsible for managing all functions, activities and processes of a corporation. It must also be able to solve different problems, which arise out of improper management of the risks. Risk refers to the uncertainties existing in any process related to the corporation and the losses occurred during an uncertainty. The management of a corporation has to manage a reliable risk management system in the corporation for proper management of risk.

Risk management is defined as the steps taken to detect a risk, calculate the probability of occurrence of the risk and take corrective actions. Due to the uncertainties that normally occur in the product development process, the process of risk management is useful during the scheduling processes of the corporation. Risk management involves various features, such as risk assessment, risk identification, risk analysis and risk estimation for the analysis and management of risk.

Risks indicate possible future happenings and are not concerned with the effects that have been observed in the past due to these risks. Risks are identified using the following attributes:

- **Probability that an event will occur**: Events can occur at any time during the project development process. An event, for example, can occur when a project developed on one computer system is transferred to another computer system. Here, both the computer systems can create incompatibility in the hardware or project. This incompatibility causes an event to occur and is identified as risk.
- **Loss associated with the event**: The adverse impact of an event could be loss of time, loss of money and lack of expected quality. For example, there can be change in user requirements after the coding phase is complete. The change in user requirements results in the loss of control when team members develop the project according to earlier user requirements.

Note that there is no fixed time for the occurrence of risks. Hence, to keep track of risks, risk management needs to be carried out throughout the project development process. Risk management is a systematic process, which focuses on identification, control and elimination of risks. The objective of risk management is to determine the loss before risks occur and then determine the ways to prevent or avoid the adverse impact of risk on the project. Risk management depends on the number and complexity of risks. Based on this, the impact of risks can be low, medium, high or very high.

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[9]http://www.tkyd.org/files/downloads/INTERNALAUDITROLEINCORPORATEGOVERNANCE.doc

Uncertainty and constraint

Risks are a combination of uncertainty and constraints. To minimize the risks, either constraint or uncertainty or both can be minimized. Generally, it is observed that it is difficult to minimize constraint, so uncertainty is reduced. Note that it is difficult to develop a project in which all the risks are eliminated. Therefore, it is essential to minimize the effect of risks, as they cannot be eliminated completely. For this purpose, effective risk management is required. Figure 3.7 shows the curved line that indicates the acceptable level of risk, depending on the project.

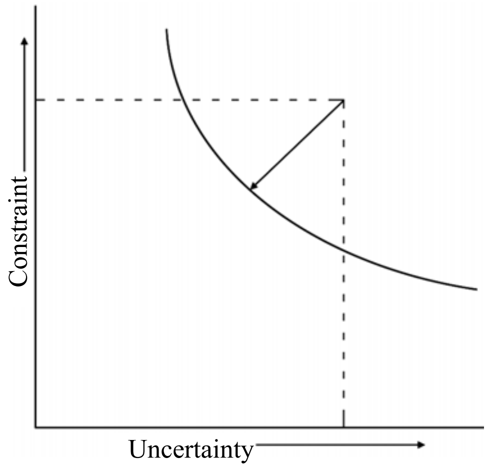

Figure 3.7: *Minimizing Risks in a Project*

Risk is associated with the uncertainties existing in a project and the losses occurred during an uncertainty. Risk management is defined as the steps taken to detect a risk, calculate the probability of occurrence of the risk and take corrective actions. Due to the uncertainties that normally occur in project development, the process of risk management is useful during project scheduling. Various steps involved in risk management are:

1. Identify the probable risks that can occur during the project duration.
2. Calculate the probability of occurrence of a risk and the possible damage caused by the risk.
3. Provide ranking to the risks identified, in order of the probability of occurrence of the risks and the severity of damage caused by the risks.
4. Develop a plan to handle risks that have a high ranking.

The plan to handle risks involves making the Risk Mitigation, Monitoring and Management (RMMM) plan and developing the risk information sheet. The risk strategies implemented by the management team are:

- Proactive risk strategy
- Reactive risk strategy

The proactive risk strategy involves the identification of risks in advance and taking corrective actions to avoid the risks. The proactive risk strategy is based on the preventive action of a risk. The reactive risk strategy includes allocating resources and taking corrective actions when a risk occurs. This strategy allocates the resources necessary to deal with the risk.

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Risk analysis

Risk analysis discovers the possible risks by using various techniques. These techniques include decision analysis, cost-risk analysis, schedule analysis and reliability analysis. After a risk is identified, it is evaluated in order to assess its impact on the project. Once the evaluation is done, risk is ranked according to its probability of occurrence. After analysing the areas of uncertainty, a description is made, which assists in how these areas affect the performance of project.

Principles of risk management

Every corporation is subjected to risks. It is essential to manage the risks to prevent losses in a corporation. If the risks are not managed, it results in project failure. Failure to manage risks is usually the result of the inability to do the following:

- Determine the measures used for managing risks.
- Determine when risk management is required.
- Identify whether risk management measures are taken or not.

Risk management is necessary because without the elimination of risks, projects cannot be developed properly. There are several principles that help in effective risk management. These are listed below:

- **Maintain a global perspective**: Risks should be viewed in relation to the project, considering all the aspects of constraints and uncertainties in it. In addition, the impact of risks on business should be considered.
- **Have a forward-looking view**: Risks that may occur in future should be assumed.
- **Encourage communication**: Communication should be encouraged among the team members of the project to increase understandability of the concept, thereby reducing the number of risks associated with the project.
- **Develop a shared project vision**: Both the project management team and the senior management should be able to view the project and its risks in terms of the common objective, say, that of developing quality project and preventing loss. By following this approach, better risk identification and assessment is achieved.
- **Encourage teamwork**: The skills and knowledge of every person involved in risk management should be combined when risk management activities are performed.

Risk management comprises of two activities, namely risk assessment and risk control. These activities identify the risks and determine ways to eliminate them or reduce their impact.

Risk assessment

Risk assessment concentrates on the occurrence of risks depending on their nature, scope and timing. The nature of risks specifies the problems that arise when a risk occurs. The scope of risks specifies the capability of risks to affect the project. Timing of risks considers when and for how long the affect of risk is observed. With the help of proper risk assessment, risks could be prevented. It is important to provide information according to the level of risks. With complete information of risk assessment, the probability of occurrence of risks and its severity is determined.

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Generally, risk assessment can be carried out any time during the project. However, it is better to begin risk assessment as soon as possible in the development process. To effectively perform risk assessment, the management should consider the occurrence of risks instead of assuming that no risks will occur during project development. In addition, a record of risk assessment should be maintained during the process. For understanding the severity of risks, which is termed as low, high or very high, earlier documents should be used as a reference and compared with the risks being assessed in the present project. Figure 3.8 shows the risk assessment process.

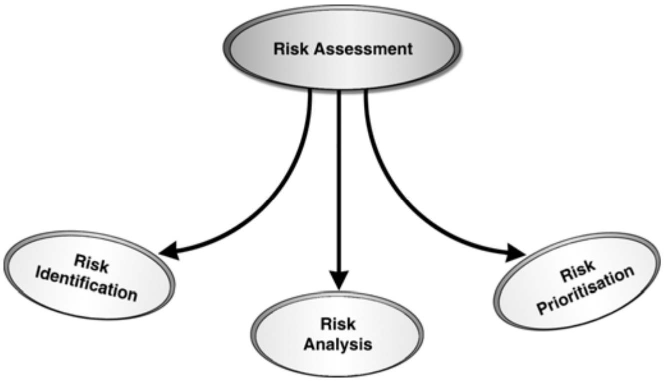

Figure 3.8: *The Risk Assessment Process*

Risk assessment comprises three functions, namely risk identification, risk analysis and risk prioritization. Risk identification is used to identify the different risks that impact the project. Risk analysis uses different techniques related to decision analysis, cost risk analysis, schedule analysis and reliability analysis to analyse the different types of risks involved in the project. Risk prioritization is responsible to manage various risks according to their effects on the projects.

Classification of risks

The risks occurring in a project are classified according to the degree of uncertainty and the extent of loss associated with the risk. The various types of risks in project management are:

- **Project risk**: These risks are the risks that cause delays in the project schedule and increase the cost of the project. These risks include uncertainties associated with the project schedule, client requirements, resources, human resource allocation and the budget of the project.
- **Technical risk**: These risks are risks that affect the effectiveness of the project that is being developed. Technical risks include uncertainties associated with the implementation of the project, interfacing, designing and other maintenance problems. These risks can also arise due to technical uncertainties, such as problems in the integration of two project modules.
- **Business risk**: These risks are the risks that affect the usability of the project. Business risks include the following risks:

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- o Losing the demand of a good project in the market. This is also called market risk.
- o Developing a project that does not go in accordance with the business strategy of a company. This kind of risk is called strategic risk.
- o Developing a project that the marketing team of the company is unable to sell.
- o Developing a project by changing the schedule for work allocation to the personnel. For example, when the management decides to handle the project with the junior staff ignoring the effort of the senior personnel. This kind of risk is called management risk.
- o Developing a project due to the lack of personnel support or economic support in the form of the budget of the project. These risks are called budget risks.

- **Known risk**: These risks are the risks that are identified and rectified after making a thorough investigation of the prepared project plan and the technical and market situations. These risks include problems, such as poor programming of the project and lack of proper planning for the dates of project completion.
- **Predictable risk**: The predictable risks are those that are identified from the past experiences of the project. The predictable risks include risks, such as the risks involved in the sudden change of personnel allocation and the lack of good communication with the client.
- **Unpredictable risk**: These risks are not predictable in nature and are not easily identifiable.

For each of the risks specified above there is another classification—product-specific risk and generic risk. The product-specific risks are traced by personnel with the knowledge of the project environment and technology. Generic risks are those that are easily traceable.

Risk identification

Risk identification is the process of detecting risks or threats occurring in the process of project development. The threat can be on the basis of the aspects of the project such as resource allocation and planned schedule of the project. The process of risk identification starts with identifying the known and predictable risks. The project manager identifies the product-specific risks by studying the planned project schedule and the statement of scope of the project to be developed.

Risk identification helps identify the events that have an adverse impact on the project. These events could be the changes in user requirements and the development of new technologies. In order to identify the risks, inputs from project management team members, users and management are considered. The project plan including the subplans should be carefully analysed in order to identify the areas of uncertainty, before starting the project. There are various kinds of risk that occur during the project development process.

The risk identification process is performed by preparing a list of risks and checking for their occurrence throughout the process of project development.

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This list of risks is called the risk item checklist. The checklist involves a set of predictable risks, which are generic in nature. The various risks mentioned in the checklist are as follows:

- Risks associated with the size of the project developed
- Risks associated with conditions prevalent in the market and other management constraints on the project
- Risks associated with the sophistication of the client to specify the requirements and risks caused due to the communication gap between the project manager and the client
- Risks associated with the planned schedule for the project development
- Risks associated with the tools used in project development
- Risks associated with the complexity of the project to be developed and the complexity of the technology used for development
- Risks associated with the experience of the personnel involved in project development

A project manager assesses the probability of the occurrence of risks in a project by answering questions such as:

- Are the senior personnel of the development team assigned the critical activities of project development?
- Is the project being developed, useful to the end users?
- Are the project requirements clear to both the project development team and clients?
- Is the scope of the project considered stable?
- Are the clients clear in defining their requirements or have they missed some requirements?
- Are the requirements of end-users of the project realistic?
- Does the personnel involved in developing the project make a skilled team?
- Have all the requirements of the process of project development been met?
- Does the personnel have knowledge about the technology involved in project development?
- Does the number of personnel employed for the project fulfil the requirements of the project?
- Is the client fully satisfied with the development of the project?

When the answer to any of these questions is no, then it means that the project manager has to start with the RMMM plans. The impact of the risk is computed using the effect, which a risk driver produces on the risk components. The types of impact of a risk based on the decreasing order of severity are:

- **Catastrophic**: It causes the cancellation of the project.
- **Critical**: It has a great impact on the project.
- **Marginal**: It has an impact on the project, which can be controlled.
- **Negligible**: It has a minor impact on the project.

NOTES

Risk estimation and exposure

Risk estimation is the process of rating the risk according to the probability of its occurrence and the consequence associated with its occurrence. Risk estimation is also called risk projection. The primary objective of risk estimation is to rank the risks according to their capability and their impact on the project. This order is decided by the project planners who along with technical and other managerial staff perform the following four steps:

1. Setting up a scale that reflects the likeliness of occurrence of a risk
2. Determining the affects of the risk
3. Calculating the impact of the risk on both the project and the final product
4. Maintaining a record of the overall accuracy of the risk projection in order to avoid any type of misunderstanding

All the above-mentioned steps help prioritize the risks. The project manager of a project performs risk estimation by preparing a risk table. The risk table contains the various risks, a categorization of the risks, the probability of occurrence of the risk, the impact of the risk on the risk components and the RMMM plan to counteract the risk. The project manager lists down the risks by consulting the risk item checklist. The risks are classified according to business risk and market risk. Each member of the project development team calculates the probability of occurrence of these risks. The probabilities calculated by each team member are then compared with each other until the values of the probability turn out to be the same.

The risks in the risk table are then placed in the decreasing order of priority. The risk with the highest probability and highest impact is listed first and the list is followed by the risks of lower impact and lower probability. This process of arrangement of the table is called first-order risk prioritization. The project manager then defines a cutoff line such that only the risks above the cutoff line are under consideration. The risks placed below the cutoff line are evaluated again and a second-order prioritization is established. The risks above the cutoff line are provided with their RMMM plans and risk information sheets.

The nature, scope and timing of occurrence of the risk affect the impact of the risks. 'Nature' refers to the types of problems which arise when the risk occurs. 'Scope' refers to the extent of harm that is produced when the risk occurs. 'Timing' of the risk is concerned with the duration of the impact of the risk.

Thus, all the possible types of risks are listed initially in the risk table. After this, each risk is categorized followed by the probability of their occurrence. Finally, each risk is scaled on the basis of their impact.

Once the risk is scaled, the risk exposure is computed for each risk mentioned in the risk table. The determination of risk exposure is done with the help of statistically-based decision mechanisms. These mechanisms specify how to manage the risk. The risk that has a greater impact on project needs to be eliminated. On the other hand, the risks that are minor and have no or little impact on the project can be overlooked.

Risk Mitigation, monitoring and management

The process of risk mitigation, monitoring and management includes the preparation of RMMM plans or the maintenance of the Risk Information Sheets (RIS) for individual risks. The RIS for the risks are maintained using a database. The database enables the comparison of data and rearrangement of the risks in the risk table during the process of risk estimation. The RMMM plan includes all the documents relevant to perform risk analysis. The strategy planned for counteracting the risks has three major aspects, which are:

- Avoiding risks
- Monitoring risks
- Managing risks

When the developing team prepares a proactive risk strategy, the importance is more towards avoiding the risks. The risk strategy includes framing a plan for risk mitigation. Risk mitigation minimizes the impact of risks. For this purpose, risk mitigation techniques are used, which are based on the occurrence of risks and their level of impact. Risk mitigation techniques incur additional cost on extra resources and time, which are required to complete the project. To avoid this, a cost benefit analysis should be done to evaluate the benefits of eliminating the risks or minimizing their impact along with the costs required to implement risk management. Appropriate measures should be taken before the risks occur, which later resolves the effect of risks when the project is in progress.

When the project is under process, then the goal of the project manager shifts to risk monitoring. The process of monitoring involves monitoring the factors that enhance the probability of occurrence of a risk. Risk monitoring contains the study of the effectiveness of risk mitigation steps. By monitoring the documentation standards, the project manager ensures that each of the documents being developed is individually readable. Therefore, when a new staff member is recruited to the project, the staff members do not face any problems in understanding the documents prepared.

Thus, risk monitoring observes the risk of a project so that appropriate techniques can be applied when risks occur. The techniques used for risk monitoring include milestone tracking, tracking the risks that have greatest impact and continual risk re-assessment. For risk monitoring, the project management team members first prioritize the risks and then they observe them. When the risks are identified, their effects are recorded by which the risks can be easily managed during the project.

When the risk mitigation plans fail and the risk finally occurs, the project manager proceeds with risk management. For example, if certain members of a project leave, then risk mitigation plans are followed and a backup plan is used to counteract.

The risk management plan describes the process of assessing risks that may occur during the project development process. Risk management is concerned with determining the outcomes of risks before they happen and specifies the procedures to avoid them and minimize their impact. It is important to consider the risks associated with a project, as it helps in determining the ways to manage them when they occur. This in turn saves time and effort required for the project development. Figure 3.9 shows the various steps included in risk management plan.

NOTES

1.0 Statement
2.0 Objective
3.0 Roles and responsibilities
  3.1 Process Task Name
  3.2 User
  3.3 Project Manager
  3.4 Software Development Team
  3.5 Sponsor
4.0 Purpose
5.0 Risk Process
6.0 Risk Management Worksheet
  6.1 Risk Management Log

Figure 3.9: *Steps in the Risk Management Plan*

The risk management plan comprises the following steps:

- ***Statement****:* It describes the purpose and advantage of identifying and recording risks.
- ***Objectives****:* It describes the activities and procedures that are followed to manage risks.
- ***Roles and responsibilities****:* It specifies the roles and responsibilities for the project management team and sponsor. In addition, users are also involved during risk management.
- ***Purpose****:* It specifies the purpose of the process for risk management.
- ***Risk process****:* It specifies the stages of risk management process and provides a process diagram to display risks for easier identification and management.
- ***Risk management worksheet****:* It specifies the risk management worksheets the such as risk management log.

The steps of the RMMM plan incur some additional project costs due to the cost of the backup. Another function of risk management involves the cost and benefit analysis of the backup plans. The cost and benefit analysis refers to analysing whether the extra project costs incurred due to the RMMM plans are small as compared to the benefits it provide.

To resolve the risks, it is important to consider the areas of the project where risks can occur in the process of project development. After determining the areas, different techniques are used for risk resolution. Generally, the techniques followed for risk resolution include estimation of cost and schedule of project, quality monitoring, evaluation of new technologies and prototyping. The risks that have a very high impact should have an emergency plan that helps in avoiding risks and minimizing the impact of the risk before they could happen.

CHECK YOUR PROGRESS

11. What is the main objective of risk estimation?
12. How does a project manager ensures the individual readability of documents?

NOTES

3.6 SUMMARY

It is clear that the management has the power to affect the behaviour and decision-making capability of the employees, as management itself is a decision-making process. Decision-making can be done under risk, certainty or uncertainty. In any situation, the process of decision-making is fraught with problems like paucity of time, weak communication, lack of sufficient information and lack of knowledge.

An organization cannot do without corporate governance which is the act of controlling, directing, and evaluating the activities of an organization needless to say that ethical decision-making forms an integral part of corporate governance today.

3.7 ANSWERS TO 'CHECK YOUR PROGRESS'

1. This model has the following three phases:
   - Intelligence
   - Design
   - Choice
2. There are three frameworks for ethical decision-making. These frameworks are:
   - Consequence-based decision-making
   - Duty-based decision-making
   - Virtue-based decision-making
3. The different characteristics of a good decision-making are:
   - Decision problems should be grabbed by the management both in space and time. This means, the decision problem should be analysed thoroughly by the management.
   - The decision made by the decision-maker should keep him in a state of calm.
   - Decisions made by the management should contribute to harmony in the organization.
   - Self-interest and self-orientation should not come in the way of decision-making.
4. The factors affecting decision-making are:
   - Programmed versus non-programmed decisions
   - Information inputs
   - Prejudice
   - Cognitive constraints
   - Attitudes about risk and uncertainty
   - Personal habits
   - Social and cultural influences

NOTES

5. The various steps in decision-making are:
    - Perception and diagnosis of the problem
    - Generation of alternate solutions
    - Evaluation of alternatives and selecting a course of action
    - Implementation of the decision
    - Monitoring feedback
6. Corporate governance can be defined as an act of controlling, directing and evaluating the activities of an organization.
7. Board of directors is made up of the individuals elected by a corporation's shareholders to look after the management of the corporation.
8. Corporate governance includes principles such as honesty, trust, integrity, responsibility, accountability and commitment to the organization. It also includes rights and equitable treatment of shareholders, interests of other stakeholders, role and responsibilities of the board, integrity and ethical behaviour, disclosure and transparency.
9. The various skills that the managers must possess are:
    - Technical skills
    - Human skills
    - Conceptual skills
    - Diagnostic skills
    - Communication skills
    - Political skills
10. The leader of an organization must possess the following qualities:
    - **Smartness**: A leader should be smart enough to solve the problems of employees.
    - **Knowledge of business**: A leader should have a good grasp of business, and the organizational goals should be clear in his mind.
    - **Decisiveness**: A leader should be a good listener, that is, he should take a decision after taking the opinion of employees.
    - **Willingness to admit mistakes**: A leader should accept all the mistakes and learn from them in order to maintain his dignity.
    - **Innovative**: A leader should be innovative in order to meet various environmental changes.
11. The primary objective of risk estimation is to rank the risks according to their capability and their impact on the project.
12. By monitoring the documentation standards, the project manager ensures that each of the documents being developed is individually readable. Therefore, when a new staff member is recruited to the project, the staff members do not face any problems in understanding the documents prepared.

3.8 EXERCISES AND QUESTIONS

NOTES

1. What is the importance of social responsibility in a business? Explain.
2. Explain the need for corporate governance.
3. Discuss some of the new trends of the board of directors in corporate governance.
4. How can a CEO handle politics within an organization?
5. Leadership strategies are essential in an organization. Discuss.
6. 'Ethical decision-making is an integral part of the functioning of an organization'. Discuss.
7. Explain the various ethical decision-making frameworks.

3.9 FURTHER READING

Modh, Satish, *Ethical Management: Text and Cases in Business Ethics and Corporate Governance.* New Delhi: Macmillan Publishers India Ltd, 2005.

Mathur, U.C., *Corporate Governance and Business Ethics: Text and Cases.* New Delhi: Macmillan Publishers India Ltd, 2005.

UNIT 4 ETHICAL ISSUES IN THE FUNCTIONAL AREA

NOTES

Structure

4.0 INTRODUCTION

Ethical in the functional areas of any business is necessary to ensure a good rapport between the management and the employees. In fact, all functional areas, namely marketing, finance, human resources as well as information technology should follow a code of ethics so as to function well and give maximum output. Only one person alone cannot achieve this. Each employee should feel responsible and try to stand by what is right in any given situation. In other words, it should be a team effort across all levels of the organization.

4.1 UNIT OBJECTIVES

This unit teaches you about:

- The ethical issues that may arise in the various functional areas of business
- Ethics in marketing, advertising, human resources, finance and information technology
- Consumer protection in the context of electronic commerce technology

4.2 ETHICS IN THE FUNCTIONAL AREA

Ethical issues can arise in various functional areas of a business such as marketing, research and development, HRM, production and finance. Ethical issues in all these functional areas must be controlled or coordinated by the chief executive officer (CEO) of the enterprise. Figure 4.1 shows the main functional areas of a business that usually give rise to ethical issues.

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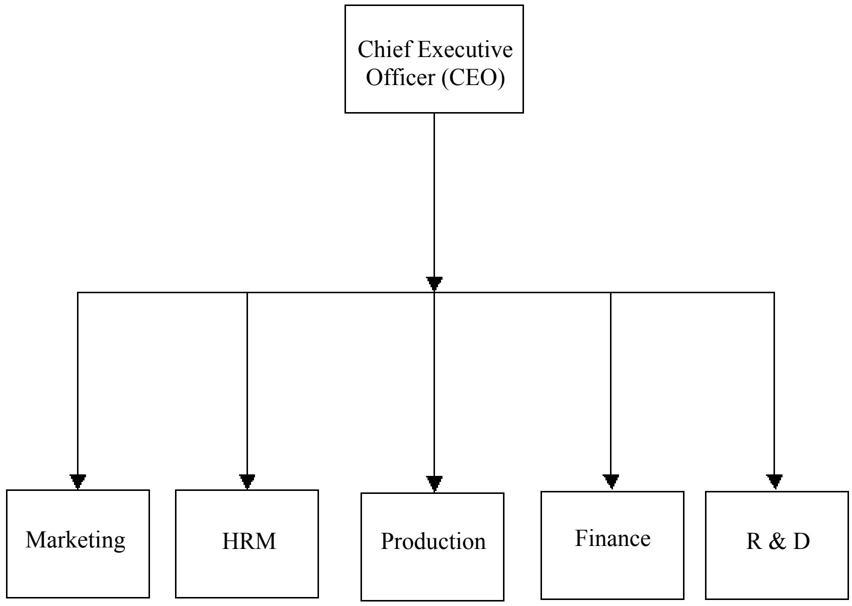

Figure 4.1: *Different Functional Areas of Business*

4.3 ETHICS IN MARKETING

Marketing is a technique that is used to attract and persuade customers. Marketing provides a way in which a product is sold to the target audience. Marketing is a management process that identifies, anticipates and supplies consumer requirements efficiently and effectively. The main aim of marketing is to make customers aware of the products and services. It also focuses on attracting new customers and keeping existing customers interested in the product. The marketing department consists of various subdivisions, such as sales, after-sales service and marketing and research. The different subdivisions of the marketing department are shown in Figure 4.2.

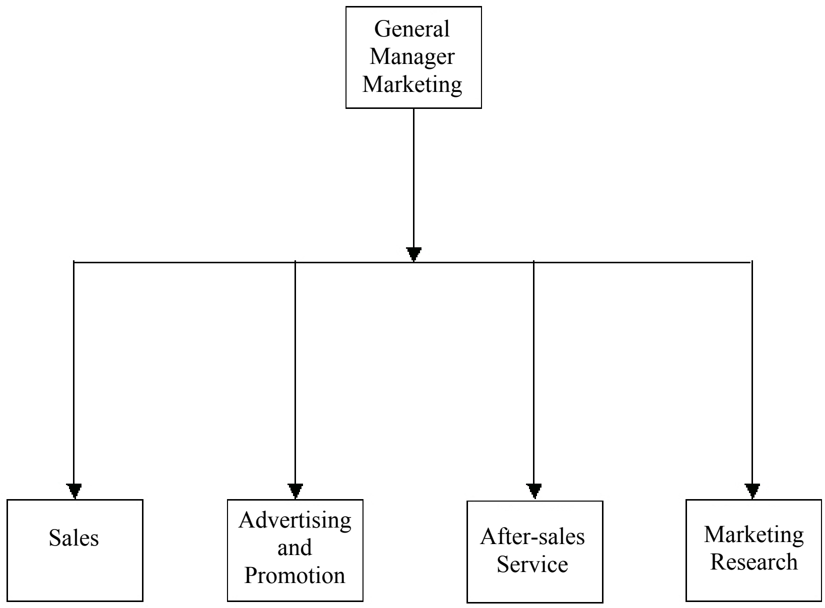

Figure 4.2: *Subdivisions of Marketing*

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In the field of sales, the following ethical issues require safeguards against unethical behaviour:

- Not supplying the products made by the company as per the order
- Not accepting responsibility for the defective product
- Not giving details about the hidden costs, such as transportation cost, while making the contract with the client
- Changing the specifications of the product without giving any prior information to the customer
- Changing the terms of the business without taking any approval from the client
- Delaying the delivery of the goods without giving any proper reason
- Treating two customers differently
- Not providing the after sales service as per the contract
- Selling the same product at different prices to different customers

Advertising and promotion provide the means for communicating with the customer. In the field of advertising and promotion, the following are examples of unethical communication practices:

- Making false commitments to the customers about the benefits of the product
- Supplying products that are different from those that are advertised
- Giving wrong prices to the customers during advertising
- Not giving the promised gift in the promotional campaign
- Hiding major flaws of the product
- Providing wrong testimonials about the product to prospective customers
- Not providing the advertised service to the customers as a part of the promotional plans
- Increasing the price of the product before starting its promotional campaign
- Making false references about the competitive products

While selling the product to the customer, a company provides some extended features or facilities along with the product, such as after-sales service. These facilities are provided to increase the sale of the product. In the field of after-sales service, the following ethical issues require safeguards against unethical behaviour:

- Using below-standard material for the service and charging for relatively better material from the customer
- Using outmoded service equipments which can be harmful for the products during service
- Not taking the service calls if the location is not easy to reach, while free service was promised before the sale of the product
- Making only temporary adjustment in the product, which can last only for a short time or to make the product useful for the time being
- Not keeping proper service records of major products for future use, as they can help in easy diagnosis of problem

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- Overbilling the service charges, when the customer is not aware of the actual rates
- Using rejected or below-standard components for customer's temporary relief
- Refusing the service of the product due to personal reasons
- Exchanging healthy parts with below-standard parts when the product comes for servicing

Marketing research is done to find out the needs of the market, its trends and competitive activities. In the field of marketing research, the following are example of unethical behaviour:

- Research is conducted only to substantiate the viewpoint of the manager.
- Research is focused on the areas that do not need to be covered.
- Some old research is presented as the new one just for the purpose of financial gain.
- A biased research report is prepared to suit the marketing manager.
- The research report is sold to the competitor.
- The report does not include important facts.

4.3.1 Ethical Issues in Advertising

In the advertising field, the ethical issues include decisions on what business and market a corporate organization should enter. Another ethical issue can be the decision on what product should be provided by a corporate organization to its customers. Though it is important that ethical standards be provided for the advertising of a particular product, it is not easy to establish common ethical standards which are agreed upon by different organizations. According to Ferrel and Gresham, 'There is no clear consensus about ethical conduct; that ethical standards are neither absolute nor constant; and that attempts to determine whether particular marketing activities are ethical or non-ethical cannot produce a definitive code of marketing behaviour'.

However, there is a general view also related to ethics in advertising. This view is that advertising practices, such as deceptive advertising, price fixing, holding of product test data, and falsifying research behaviour in the market are unethical practices.

In the advertising field, marketing promotion is the area where a large amount of public scrutiny takes place. Media persons report immediately any lack in ethical standards while selling products, in public relations and advertising. Organizations follow various methods that are unethical while advertising for their products and services. These methods are:

- Ambiguity
- Concealed facts
- Exaggeration
- Psychological appeal

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Ambiguity

Ambiguous advertisements are mostly deceiving for customers. Advertisements become ambiguous when they are wrongly interpreted and also with, the use of words through which organizations can avoid making direct statements. For example, you can consider the word 'help'. This word is used by organizations to ambiguously advertise their products. It can be used in the following ways in advertisement:

- Help us keep young
- Help you improve your complexion
- Help prevent cavities
- Help keep our house insect free

Organizations must provide clear information about products even though their advertisements can be interpreted differently by individuals. Ambiguity in advertisements can affect the health, loyalty and expectations of people who will be purchasing the product that has been advertised.

Concealed Facts

Organizations can conceal information related to a product that may result in less selling of that product thereby resulting in loss. The advertising practice of concealing facts is unethical because it, in a way, allows the exploitation of people. There are mainly two considerations regarding advertisements that force organizations to conceal facts. The first consideration is that information that will help in selling a product in the best way should be provided. The second consideration is that the information about a product should be provided in such a manner that:

- Individuals, who will be purchasing the product do not feel that false promises have been made to them and that they have been let down.
- Advertisements related to a product are able to avoid objections from agencies that are responsible for monitoring advertising.

Organizations may conceal facts that may be important in fulfilling the needs of customers. This way the organizations may be exploiting the customers and causing serious health injuries to them. Customers may also not be able to obtain the products of their choice.

Exaggeration

Organizations may mislead the customers by providing exaggerated information in the advertisements of their products. The exaggerated information is information that is not supported by evidence. Organizations can exaggerate information in advertisements by using superlative phrases. For example, an organization manufacturing pain relief ointments, can exaggerate information by stating that a pain reliever provides extra pain relief. The use of these superlatives may not cause any harm to customers but may be misleading sometimes. For example, if a washing powder manufacturing organization uses the phrase, 'best loved by housewives' then no harm may be caused to consumers of washing powders.

CHECK YOUR PROGRESS

1. What are the various sub-divisions of the marketing department?
2. Give some examples of unethical communication in advertising.

NOTES

Psychological Appeal

A psychological appeal is the appeal made considering the emotions of customers. The main objective of psychological appeal is to persuade customers to purchase products by appealing to their emotions and not to reason. For example, consider a car advertisement which focuses on the desire of the elite class to achieve status. Similarly, a life insurance company may use emotions, such as pity and fear in its advertisement to persuade people to take insurance policies. Through psychological appeal, the organizations make promises about their product that are not fulfilled when customers buy the products.

4.3.2 Ethical Issues in Takeovers and Mergers

Mergers and takeovers are stimulated by the urge to diversify or to anchor the new market rather than to dominate an industry. This diversification may decrease overhead costs or protect the organization from economic descent in its actual industry. A takeover may come from within the organization with help from an external source. The primary goal of the corporate investor is profit of the shareholders, so even they may be convinced by the idea of the replacement of the top management. There are certain events that lead to mergers:

- Lack of funds to compete with organizations with better facilities, new equipments and a large workforce.
- A growing number of competitors who have recovered from their respective economic conditions with the help of mergers and acquisitions.
- Liberalization has weakened the economy in many Indian organizations as they have not been able to adjust with the competitive market.
- Due to technological advancements, there is technical competition making it difficult to attain economies of scale and to retain skillful personnel.
- Emergence of multinationals that have substantial resources to pose a challenge to the market share of Indian organizations.

The Merger Process

Every merger and takeover has certain characteristics. The merger process involves:

- The decision to consider options of merging
- Search of a suitable merger partner
- The decision to merge with a specific partner
- Making a proposal to a suitable partner
- Negotiation of merger agreements
- Formulation of implementation plans
- Accomplishing the implementation plan
- Review and evaluation

Issues during the merger process

Some organizations are not prepared to face issues and problems that come up during the merger process. They barely have a systematic and expansive process for planning and implementation due to the following reasons:

- Often, the steps taken during the merger are in response to internal and external stress. So, there is always the question of whether the merger will be able to achieve the organizational objectives.
- As average organizations do not have experience in mergers, it is tough for them to identify their problems and formulate alternatives.
- The initial problems that follow mergers mark a chain of events that affects jobs and work assignments. The top management neglects the long-term effects on relevant stakeholders under the pressure of mergers.
- Mergers lead to new organizations with new management structures, so it becomes difficult to determine directions and policies.

Hostile Take-overs

Mergers and takeovers seem friendly but they are increasingly evolving into bitter conflicts. This is due to the reason that the top-level managers want to ensure that they are saved in the event of a merger. A merger can be referred to as the coming together of two organizations in their mutual interests and combining to form a large organization. In case of a conflict, one organization takes over an unwilling partner, which is called a hostile takeover. The first group may disagree with the existing policies of the organization. Their aim would be to replace the top management with the people who share their concerns and will implement the required changes. Sometimes, they may want to take over the management to run it efficiently and to save jobs. To prevent such discrepancies, many organizations adopt complex defensive strategies. These strategies are made keeping in view organizational laws and designed in order to wear down the potential of the aggressors. This strategy may be short-term or long term, but may sometimes weaken the financial liquidity of the organization.

4.4 ETHICS IN FINANCE

Finance is an important element of an organization and it helps in its growth and development. Finance plays an important role in making resources available in an organization, such as man, machine, material, market and money. The finance manager of the firm is responsible for arranging the finances for the firm. The finance manager can raise funds from the following two sources:

- **Internal Sources**: Internal sources means the owner's own funds that are invested as equity in the organization. In case of small organizations, the owner's contribution in terms of equity is low. Therefore, large amount of money is raised from external sources. The entrepreneur can raise finance internally from various sources:
    - Deposits and loans given by owner
    - Personal loan from provident fund and life insurance policy
    - Funds accumulated by the retention of profits
    - Ploughing back of profits
- **External Sources**: External sources means the various financial institutions from where entrepreneurs can raise funds, such as fixed capital, commercial banks and development banks. The entrepreneur can raise finance by:

CHECK YOUR PROGRESS

3. How can an entrepreneur raise funds internally?
4. What are the unethical methods followed during advertising?

o Borrowing money from friends and relatives
o Borrowing from financial institutions

Figure 4.3 shows the organizational chart for the finance function.

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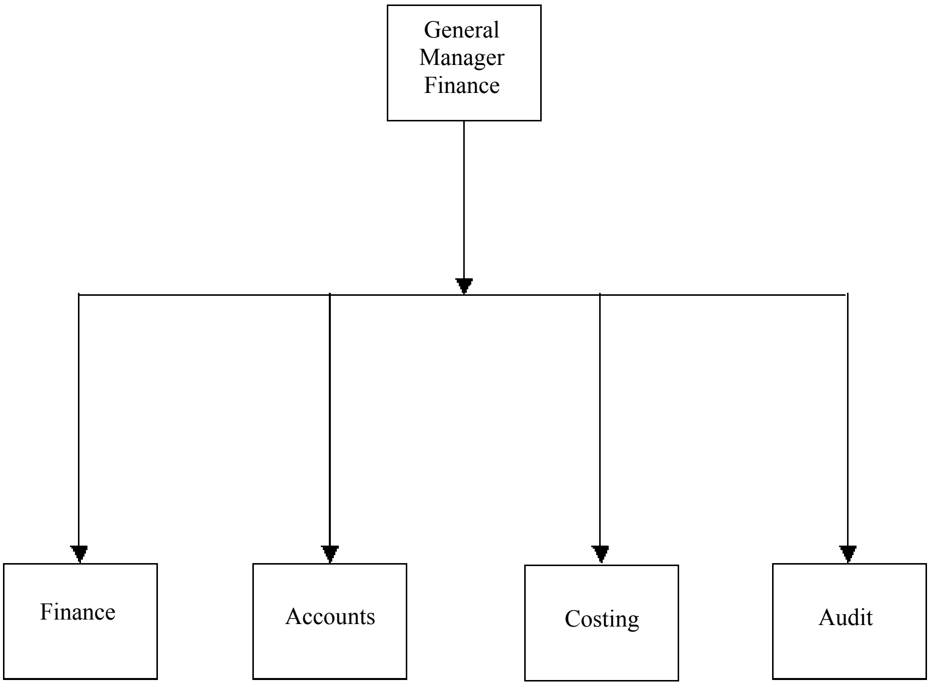

Figure 4.3: *Organizational Chart for Finance Function*

The finance department of an enterprise is prone to the following unethical practices:

- Overestimating promoters' capital utilization
- Overbudgeting project costs
- Using underhand tactics with the financers to gain benefits for the firm as well as for themselves
- Purchasing capital equipments at a time when there is no requirement for it
- Selling the capital equipments in order to raise additional and unaccounted funds
- Siphoning funds for the promoter's personal benefit
- Investing unapproved funds in order to gain extra profits
- Claiming insurance cover for losses that never happened
- Overpricing the current assets in order to gain more working capital than permitted
- Using working capital funds for personal gains

The accounts department of an enterprise is prone to the following types of unethical issues:

NOTES

- Showing inflated salaries and getting receipts from employees for an amount larger than what they actually get
- Playing inflated vendor bills in order to get discounts or commissions
- Paying overtime wages when there in no requirement for them
- Maintaining two different sets of books, one for the management and the other for income tax
- Refusing to reject unacceptable raw materials when the vendor bills have to be paid
- Delaying the clearance of the bills payable in order to get maximum interest for the amount to be paid
- Allotting extra travelling allowances to favourite employees
- Showing wrong figures in the monthly trial balances for personal benefits

The following are the unethical practices of the costing manager:

- Reducing manufacturing costs by manipulating work hours
- Ignoring cost of rejects
- Ignoring cost of rework
- Not accounting for man-hours lost due to strikes and absenteeism
- Not accounting for man-hours lost in maintenance work
- Not considering the work stoppages due to change in models
- Ignoring the man-hours lost due to change in the manufacturing process
- Ignoring time lost in failed experimentations
- Not taking into acccount the benefits of economies of sales and experience curve

The following points describe the unethical behaviour of the auditing manager:

- Ignoring major deviations from the budgets
- Rejecting the tender having lowest cost among all due to personal reasons
- Helping in hiding black money in order to reduce the tax payable amount
- Ignoring inflated travel bills of selected employees
- Accepting payments made by the directors for personal purchases as official payments
- Enabling the directors in sending and receiving money from overseas through unofficial hawala channels
- Approving payments to suppliers without checking bills or deliverables
- Approving the substandard construction made by the constructor and approving their bills for payment

4.5 ETHICS IN HR AND INFORMATION TECHNOLOGY

NOTES

4.5.1 Ethics in Human Resource Management (HRM)

HRM is concerned with the management of the 'people' of an organization. The term HRM is used to refer to the procedures, philosophy, policies, and practices related to the management of people within an organization. HRM is an approach to bring the people and the organization together so as to achieve the desired goals. It helps in creating a relation between the management of the organization and the employees which is based on cooperation and coordination according to the designed strategy. It is the art of promoting, developing and maintaining a competent workforce to achieve the goals of an organization in an effective manner. HRM is responsible for performing various functions like planning, organizing, directing and controlling of human resources. HRM also involves activities like procurement, development, compensation and maintenance.

According to Ivancevich and Glucck, 'Human resource management is the function performed in organizations that facilitates the most effective use of people (employees) to achieve organizational and individual goals.'

HRM is extensive in nature and it is present in all organizations and at all levels of an organization. HRM focuses on action rather than theoretical procedures and it encourages an employee to utilize his skills and potential completely to give his best to the organization. It encourages the employees through systematic procedures like recruitment, selection, training and development. An effective HRM works towards achieving its goals by providing a competent and motivated workforce. The primary aim of HRM is the promotion of effectiveness of the people employed in the organization and the performance of their allotted duties with cooperation. It seeks to develop and bring together an effective organization, enabling the women and men who make up an enterprise to give their best contribution towards its success both as members of a working group and as individuals . HRM can help organizations achieve their goals more effectively and efficiently. Effective management of human resources helps in improving the quality of work life. It seeks to provide fair conditions and terms of employment and work that satisfies all those employed. The following are the key objectives of HRM:

- To recruit trained and spirited employees
- To help the organization reach its goals
- To train the employees for best results
- To communicate HR policies to the employee
- To ethically respond to the needs of the society

Figure 4.4 shows the organizational chart for HRM.

CHECK YOUR PROGRESS

5. What could be the unethical practices of the auditing manager?
6. What do you understand by external sources of funds?

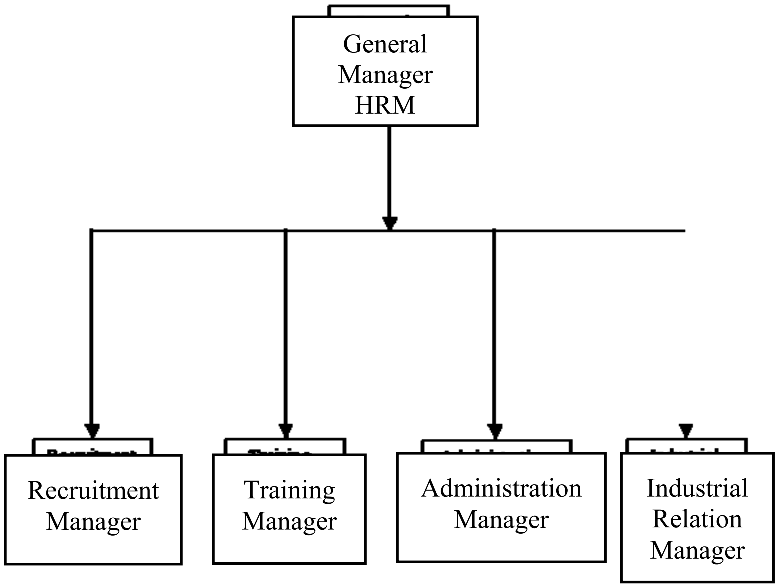

Figure 4.4: *Subdivisions of HRM*

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The following are examples of unethical practices during the recruitment process of a company:

- Recruitment of known persons without assessing their abilities
- Recruitment on the basis of financial favours
- Recruitment of the relatives of other employees
- Recruitment based on the recommendations of friend, business associates and other persons close to the leader
- Recruitment of underqualified persons
- Recruitment of overqualified persons
- Recruitment of less acceptable men when there are better suited women available for the job.
- Employing children below fourteen years for the job
- Giving less than minimum wages fixed by the government

The training manager of the company can also indulge in unethical practices as can be seen from the following points:

- Arranging training only for favourite employees, whether they deserve it or not
- Employing outsiders for providing training to trainees even when there are several persons available inside
- Planning and organizing the training programme without even knowing the need for training
- Organizing training during peak seasons or on days when workload is very high
- Starting training programmes in an ill-prepared manner
- Extending the time of the training programme to allow the trainees to have a relaxed time

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- Supplying outmoded and old training materials for the purpose of training
- Experimenting with trainees by asking them to set their own timetable for training

In the area of administration, the following are the unethical practices the manager can indulge in:

- Tampering leave records of the employees
- Giving leaves continuously to favourite employees
- Giving promotions to non-eligible persons merely on the recommendations of a friend or business associate
- Ignoring issues related to the security of the company
- Interference in various activities of the administration from the top management
- Giving the contract for uniforms of the employees to the wrong companies just for the sake of personal benefits

4.5.2 Ethics in Information Technology

Information technology refers to the gathering, processing, creation, delivery and storage of information and all the processes that make all this possible. The volume of work that is handled using IT continues to increase almost everyday. Whatever be the field, one is sure to find IT at work.

Information technology is new to the world in which the clear legal environment is yet to develop, so getting benefits by using IT cannot be surely ethical or legal. Therefore, when we talk about ethics and IT, many new problems crop up.

The characteristic of IT is that it is a particular field which has no geographical boundaries but application of IT may affect culture and environment differently. The features which are acceptable in one culture may be unethical in another.

Computer ethics was founded by MIT Professor Norbert Wiener in the early 1940s when he was providing a helping hand in the development of an aircraft cannon, capable of gunning down fast-moving war planes. Wiener created a new branch of science called cybernetics—the science of information feedback. By combining cybernetics with digital computers, he foresaw revolutionary social and ethical consequences.

Technology Ethics: Technology ethics is a new subject. The profile of technology ethics is as follows:

1. Thinking ethically about human biotechnology.
2. Taking responsibility for e-wastage like environmental damage from computer and other electronic wastages.
3. Employers must check whether employees are wasting time at recreational websites or sending unprofessional e-mails.
4. Sometimes the invasions of piracy occurs through to use of the Internet services.

CHECK YOUR PROGRESS

7. Can the training manager also indulge unethical practices?

Wiener was of the view that the integration of computer technology into society would have a great impact. New computer crime laws and privacy laws had been enacted in Europe and America by the mid-1970s. Walter Maner innovated a separate branch of applied ethics—'computer ethics' which he defined as the branch of applied ethics which studies ethical problems — transformed, aggravated, or created by computer technology. Computer ethics has been described in the following manner by James Moor: 'A typical problem in computer ethics arises because there is a policy vacuum about how computer technology should be used. Computers provide us with new capabilities and these in turn provide new choices for action. Often, either no policies for conduct in these situations exist or existing policies seem inadequate.' According to Moor, computer ethics should include:

1. Identification of computer-generated policy vacuums
2. Clarification of conceptual muddles
3. Formulation of policies for the use of computer technology
4. Ethical justification of such policies

Ethical Issues: There are various ethical issues involved in information technology. In 1986, Masovi had classified ethical issues in the following four groups:

1. **Accessibility**

It involves the right of accessing the required information as well as the true payment of charges to access the information.

2. **Privacy**

It deals with the degree of privacy and dissemination of information about an individual.

3. **Property**

It talks about ownership and value of information.

4. **Accuracy**

The information which is viable and being accessed is now much more accurate and authentic.

The Computer Ethics Institute in Washington DC has laid down the following ten commandments of computer ethics:

1. You will not use computer to harm other people.
2. You will not interfere with the computer network of other people.
3. You will not snoop around in files of other people's computer.
4. You will not use a computer to steal.
5. You will not use a computer to bear false witness.
6. You will not copy or use proprietary software for which you have not paid.
7. You will not use other people's computer resources without authorization.

8. You will not use other people's intellectual output.
9. You will think about the social consequences of the programme you are writing or the system you are designing.
10. You will always use a computer in ways that demonstrate considerations and respect for your fellow humans.

4.5.3 Consumer Protection in the Context of Electronic Commerce

Recommendation of the Organization for Economic Cooperation and Development (OECD) Council Concerning Guidelines for Consumer Protection in the Context of Electronic Commerce (e-commerce).

Consumer laws, practices and policies limit misleading, fraudulent, and unfair commercial conduct. Such protection is indispensable for establishing a more balanced relationship between consumers and businesses in commercial transactions and in building consumer confidence.

The digital networks and computer technologies that comprise the electronic marketplace have an inherent international nature. This requires a global approach to consumer protection as part of a predictable and transparent legal and self-regulatory framework for e-commerce. The global network environment challenges the abilities of each country or jurisdiction to adequately address issues related to consumer protection in the context of e-commerce. Disparate national policies may impede the growth of e-commerce, and as such, these consumer protection issues may be addressed most effectively through international cooperation and consultation. OECD member governments have recognized that internationally coordinated approaches may be needed to exchange information and establish a general understanding about how to address these issues.

A variety of consumer protection laws exist that govern business practices. Many OECD member countries have begun to review existing consumer protection laws and practices to determine whether or not changes need to be made to accommodate the unique aspects of e-commerce. In April 1998, the OECD Committee on Consumer Policy began to develop a set of general guidelines to protect consumers participating in e- commerce without erecting barriers to trade. These guidelines represent a recommendation to businesses, governments, consumers and their representatives as to the core characteristics of effective consumer protection for e-commerce. In particular, the purpose of the guidelines is to provide a framework and a set of principles to assist:

- Governments in formulating, reviewing, and implementing consumer and law enforcement practices, policies, and regulations if necessary for effective consumer protection in the context of electronic commerce
- Consumer groups, business associations, and self-regulatory bodies, by providing guidance as to the core characteristics of effective consumer

CHECK YOUR PROGRESS

8. Mention Masovi's classification of ethical issues.

protection that should be considered in formulating, reviewing, and implementing self-regulatory schemes in the context of e-commerce, and

- Individual consumers and businesses engaged in e-commerce, by providing clear guidance as to the core characteristics of information disclosure and fair business practices that businesses should provide and consumers should expect in the context of e-commerce.

Guidelines

Scope: These guidelines apply only to business-to-consumer e-commerce and not to business-to-business transactions.

General Principles

1. Transparent and effective protection

Consumers who participate in e-commerce should be afforded effective and transparent consumer protection that is not less than the level of protection afforded in other forms of commerce.

Businesses, governments, consumers and their representatives should work together to achieve such protection and determine what changes may be necessary to address the special circumstances of e-commerce.

2. Fair business, advertising and marketing practices

- Businesses engaged in e-commerce should pay due regard to consumers' interests and act in accordance with fair advertising, business, and marketing practices.
- Businesses should not make any representation or omission, or engage in any practices that are likely to be fraudulent, deceptive, misleading, or unfair.
- Businesses promoting, selling or marketing services or goods to consumers should not engage in practices that are likely to cause unreasonable risk or harm to consumers.
- Whenever businesses make information available about the goods or services they provide , they should try to present such information in an accurate, clear, conspicuous, and easily accessible manner.
- Businesses should comply with any presentations they make regarding practices or policies relating to their transactions with consumers.
- Businesses should take into account the global nature of e-commerce and wherever possible, should consider the various regulatory characteristics of the markets they target.
- Businesses should not exploit the special characteristics of e- commerce to hide their true location or identity , or to avoid compliance with consumer protection standards and/or enforcement mechanisms.
- Businesses should avoid using unfair contract terms.

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- Marketing and advertising should be clearly identifiable as such. Marketing and advertising should identify the business on whose behalf the advertising or marketing is being conducted where failure to do so would be deceptive.
- Businesses should be able to substantiate any expressed or implied representations as long as the representations are maintained, and for a reasonable time thereafter.
- Businesses should implement and develop easy-to-use and effective procedures that permit consumers to choose whether or not they wish to receive unsolicited commercial e-mail messages. Where consumers have indicated that they do not want to receive unsolicited commercial e-mail messages, such choice should be respected. In many countries, unsolicited commercial e-mail is subject to specific legal or self-regulatory requirements.
- Businesses should take special care in marketing or advertising that is targeted at the elderly, children, the seriously ill, and others who may be helpless in fully understanding the information presented to them.

4.6 SUMMARY

Ethical issues are a part and parcel of any business as unethical practices can take place across the organization in all departments.

Ambiguity, concealed facts, exaggeration and psychological appeal are certain methods by which organizations may be following unethical practices while advertising. Facts are almost always concealed in advertisements, which is absolutely unethical. Similar practices are common in the finance and human resources departments also. Effective consumer laws, policies and practices can limit fraudulent and misleading commercial conduct.

4.7 ANSWERS TO 'CHECK YOUR PROGRESS'

1. The marketing department consists of various subdivisions, such as sales, after-sales service and marketing and research.
2. In the field of advertising, the following are examples of unethical communication practices:
    - Making false commitments to the customers about the benefits of the product
    - Supplying products that are different from those that are advertised
    - Giving wrong prices to the customers during advertising
    - Not giving the promised gift in the promotional campaign
    - Hiding major flaws of the product
    - Providing wrong testimonials about the product to prospective customers

- Not providing the advertised service to the customers as a part of the promotional plans
- Increasing the price of the product before starting its promotional campaign
- Making false references about the competitive products.

3. An entrepreneur can raise funds internally from various sources:
   - Deposits and loans given by owner
   - Personal loan from provident fund and life insurance policy
   - Funds accumulated by the retention of profits
   - Ploughing back of profits
4. Organizations follow various methods that are unethical while advertising for their products and services. These methods are:
   - Ambiguity
   - Concealed facts
   - Exaggeration
   - Psychological appeal
5. The following points describe the unethical behaviour of the auditing manager:
   - Ignoring major deviations from the budgets
   - Rejecting the tender having lowest cost among all due to personal reasons
   - Helping in hiding black money in order to reduce the tax payable amount
   - Ignoring inflated travel bills of selected employees
   - Accepting payments made by the directors for personal purchases as official payments
   - Enabling the directors in sending and receiving money from overseas through unofficial hawala channels
   - Approving payments to suppliers without checking bills or deliverables
   - Approving the substandard construction made by the constructor and approving their bills for payment
6. External sources of funds means the various financial institutions from where entrepreneurs can raise funds, such as fixed capital, commercial banks and development banks. The entrepreneur can raise by:
   - Borrowing money from friends and relatives
   - Borrowing from financial institutions

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7. The training manager of the company can also indulge in unethical practices in the following:
    - Arranging training only for favourite employees, whether they deserve it or not
    - Employing outsiders for providing training to trainees even when there are several persons available inside
    - Planning and organizing the training programme without even knowing the need for training
    - Organizing training during peak seasons or on days when workload is very high
    - Starting training programmes in an ill-prepared manner
    - Extending the time of the training programme to allow the trainees to have a relaxed time
    - Supplying outmoded and old training materials for the purpose of training
    - Experimenting with trainees by asking them to set their own timetable for training
8. In 1986, Masovi had classified ethical issues in information technology in the following four groups:

    1. Accessibility

    It involves the right of accessing the required information as well as the true payment of charges to access the information.

    2. Privacy

    It deals with the degree of privacy and dissemination of information about an individual.

    3. Property

    It talks about ownership and value of information.

    4. Accuracy

The information which is viable and being accessed is now much more accurate and authentic.

4.8 EXERCISES AND QUESTIONS

1. What are the ethical issues involved in information technology?
2. Unethical practices can take place during recruitment. Explain.
3. The finance department is prone to unethical practices. Explain.
4. What are the guidelines for effective consumer protection in electronic commerce?

4.9 FURTHER READING

NOTES

Modh, Satish, *Ethical Management: Text and Cases in Business Ethics and Corporate Governance.* New Delhi: Macmillan Publishers India Ltd, 2005.

Mathur, U.C., *Corporate Governance and Business Ethics: Text and Cases.* New Delhi: Macmillan Publishers India Ltd, 2005.

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UNIT 5 ENVIRONMENTAL ETHICS, CORRUPTION AND GENDER ISSUES

Structure

5.0 INTRODUCTION

Corporate governance is all about the ethical issues, morals or the value framework within which corporate decisions are taken. Financial integrity would be the most important issue as far as corporate governance is concerned. But apart from these, corporate governance is faced with problems arising out of gender issues, corruption and sexual harassment too. None of these issues are easy to check. For example, in case of corruption, the political will of the ruling management and an effective anti-corruption framework is required to control unethical practices. In most countries, especially the developing ones, it is seen that the very institutions responsible for checking corruption are themselves fraught with internal corruption. As a result, their proper functioning is compromised. Therefore, effective corporate governance would translate into transparency in functioning without compromising the business strategies required to succeed. Needless to say that considering the unethical practices rampant today, this is quite a mammoth task.

5.1 UNIT OBJECTIVES

This unit teaches you about:

- Ethics in relation to the environment
- Ethics with regard to gender discrimination
- Sexual harassment and its legal aspect
- Effect of corruption on governance

5.2 ENVIRONMENTAL ETHICS

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Environmental ethics is all about the ethical relationship between us as human beings and his natural environment.

Human beings take a lot of ethical decisions concerning the environment. These decisions could be about whether a forest area needs to be cleared to create space for humans or for human consumption, whether zero-emission vehicles should be used in order to save on fossil fuel resources, whether consumption should be cut down to preserve resources for future generations, whether it is right to be indifferent to the extinction of certain species only because it is convenient for the society, and so on.

Suppose some farmers burn and clear forest areas for cultivation, would it be possible to justify their act? Suppose a green area is totally cleared of the vegetation to make space for commercial or residential complexes, would this act be justified? Suppose a company conducts open-pit mining in some virgin territory, does the company hold the responsibility to restore the ecology of that region?

Is it right to spread awareness against pollution only because it affects human beings and not because the values of certain members of the natural environment also need to be protected? Environmental ethics is all about raising such questions and finding their answers.

Environmental movements started when the environmentalists the world over acted together to draw attention to the philosophical aspects of environment-related problems. People woke up to realize the importance of a natural ecological balance between the living and non-living entities. Activists across the globe are spreading awareness about global warming and the significance of environmental preservation.

Marshall supports three ethical approaches to classify the various attempts at explaining the significance and importance of environmental preservation — the Libertarian extension, the Ecological extension and Conservation ethics.

The first approach emphasizes on the theories that promote the application of human rights to non-human animals as well as the inanimate entities. The second approach emphasizes on the fundamental interdependence of both biological as well as abiological entities and their diversity. This classification would include the theory that earth as a planet modifies its geophysiological structure with time to be able to support the equilibrium of evolving organic and inorganic matter. The conservation approach considers only the worth of the environment, that is, the purpose it serves for human beings. In other words, conservation is solely concerned with human beings and their intergenerational considerations.

Environmental ethics as an institution gained prominence only in the1990s. Nowadays, universities offer programmes that specialize in environmental ethics and philosophy.

5.3 CORRUPTION

Corruption refers to the abuse of public office, that is, use of public office for some personal benefit. Ethical governance propagates that all are equal in the eyes of the law. But, corruption practices the exact opposite. Increasing corruption has led to a situation where only dissipation of corruption can result in equality before the law.

The root cause of corruption is moral decline. Changing lifestyles have not only affected the individual's sense of values, but also the values that were nurtured and preserved by the society. These changes have affected the system of governance.

Corruption works against the nation, against the poor strata and against the economic progress of the country.

The history of our country's governance is fraught with examples of corruption that put the nation at security risk. There have been instances of corruption in politics, in defence deals and even cases of militants being funded through Hawala.

Corruption in today's society can be linked directly with the falling morality standards. The level of corruption in any society is dependent on the following three factors. These are:

(i) The values cherished by society
(ii) The individual sense of values
(iii) The governance system (probably, at this stage, it is worth looking at corruption's social roots)

Corruption is harmful for the society in different ways. Corruption is anti-national. The Hawala scam that was exposed a few years ago has shown how the militants based in Kashmir were receiving cash from abroad through hawala channels. Through this same route politicians, businessmen and bureaucrats were also collecting money.

The nation witnessed another major scam, which was exposed by Tehelka.com. The expose highlighted the high level of corruption in defence deals. From such events, one can judge that corruption is anti-national as it threatens national security.

Moreover, corruption is anti-poor. There have been reports in the Indian media of high level of corruption in the Public Distribution System (PDS). A major portion of sugar and other food grains , which are designed to ensure food security to the population living below poverty line, goes to the black market.

The Indian Government incurs huge expenditure every year on PDS by way of subsidizing the foodgrain prices for the poor. This means that huge amounts of money lands in the pockets of the corrupt PDS shopkeepers and their godfathers in bureaucracy and politics. Out of every rupee meant for anti-poverty programmes, it is a known fact that only a fraction reaches the beneficiary. Corruption is, therefore, anti-poor.

Corruption also has another characteristic of being anti-economic to development. In mid-1997, the collapse of the South East Asian economies had shown how even the so-called tiger economies were not immune to the disastrous consequences of crony capitalism and corruption. In 1999, the Mahbub Ul Huq Centre in Islamabad in its Human Development Report for South Asia said that India's GDP will grow by 1.5 per cent and the foreign direct investment will grow by 12 per cent if the country's corruption level comes down to that of the Scandinavian countries.

Corruption can be a matter of life and death many a times. For example, spurious drugs can lead to the death of many innocent people as a result of corruption in the pharmaceutical industry. Corruption in government departments can also lead to deaths of innocent people. The 1993 Mumbai blast, in which 300 innocent people were killed was the result of RDX smuggled into the country with the support of corrupt officials in the state government. Another example of how corruption leads to death is the manufacture and sale of illicit liquor. In short, corruption is anti-economic development, anti-national, and anti-poor. The irony is that we nevertheless seem to accept corruption as a part of life.

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5.4 GENDER ETHICS

It is hard to believe that even a progressive phenomenon such as globalization can actually heighten gender inequality. It has been pointed out many a times that gender equality plays a major role in the development of a nation. However, despite modern initiatives it is disappointing to note that the situation of women all over the world has not improved significantly. This is where gender ethics takes a back seat.

Societies that still remain backward are those where women have been marginalized and where poverty has been feminized. Globalization means a situation or condition that encourages the movement of capital around the globe at a fast pace. It also implies the disappearance of tariff barriers and the spread of new information and communications technologies. But the benefits of globalization are not always equally distributed. Needless to say, the efforts to help women progress are also stunted.

It would be quite a challenge to encourage women from all over the world to participate in the whole process of globalization, because not all women enjoy freedom of movement. For those who are not even allowed to leave the four walls of their home, the need to create channels that would help throw the doors open for participation arises. In the women-friendly regions, the focus should be on creating more facilities for women to participate in different ways and at different levels in the market.

The majority of the Internet users consists of men which means women still remain far behind when it comes to benefiting from information technology. The benefits of progress, modernization and globalization have not been fairly distributed and the gap between the haves and the have nots has not been bridged. With women forming the majority of the poor in the world, this only strengthens the fact that gender inequality is certainly not a myth.

Women clearly shoulder more responsibilities than men and are also expected to play dual roles as bread-winners as well as housekeepers. This exposes them to more mental and physical stress as well as health hazards than men. The underdeveloped countries have been victims to unethical peddling of medicines that do not meet the global safety standards. Women, especially those who are pregnant are at the receiving end of all the harmful effects of these dangerous medicines. They not only risk losing their lives, but also endanger the lives of their unborn children.

In the Third World countries, often aggressive and unethical sales campaigns lead the illiterate women to believe that breastfeeding is no longer the best way to feed an infant. With declining breastfeeding rates, the state of health of women and children have been far from enviable. This is just one of the ways in which unethical practices are targeted at women.

With smoking taking a back seat in the developed countries, more and more tobacco companies are targeting the population in the underdeveloped nations to promote their products. The victims of such marketing include women too who not only risk their health, but also turn their offsprings into passive smokers. Indirectly, the wives of poor farmers who are addicted to tobacco or other forms of hazardous intoxication bear the brunt of the resulting poverty and are forced to shoulder the burden of running the family.

A look at today's best advertisement will prove to us that gender ethics has yet not been given due importance in the world today. It is here that women are exploited the most in terms of their sexuality. Most often than not, the products advertised possess no connection with the figure of the scantily-clad women displayed beside them, for example, advertisements featuring motorbikes and men's wear. These advertisements and the concept of sex tourism which has gained alarming popularity clearly reflect the manner in which women are regarded in society—their value or worth being measured merely in terms of their sexual appeal and glamour.

5.5 SEXUAL HARASSMENT AND DISCRIMINATION

In USA and UK, sexual harassment is considered to be a serious form of violence and proper legislative measures have been taken to protect women and combat sexual harassment at work.

However, in India, it has not been very long since The Supreme Court recognized sexual harassment, for the first time, as a violation of human rights and a gender-based discrimination affecting women's 'Right to Life and Livelihood'. Although mandatory guidelines for resolution and prevention of sexual harassment of women at work have been put in place, the issue of sexual harassment and discrimination still remains under carpet for most employers and women.

The Supreme Court of India defines sexual harassment as 'any unwelcome sexually-determined behaviour that includes a demand or request for sexual favours, physical contact, sexually-coloured remarks, pornography display, and any other verbal, physical, or non-verbal conduct that is of a sexual nature.

A sexually-harassed person would be one who:

1. Is subjected to an unwelcome act of physical intimacy
2. Has been asked for sexual favours in return for employment, payment of wages or a promotion
3. Has been at the receiving end of sexually explicit compliments, or sexist remarks or jokes with sexual connotations
4. Has been forced to view sexually explicit pictures, cartoons, calendars or even e-mails, etc.
5. Has been subjected to offensive gestures, sounds or any conduct of a sexual nature which could be either verbal or non-verbal
6. Has been threatened for refusing to cooperate with the person demanding sexual favour
7. Has been repeatedly asked out by the boss or forced to answer queries (by the boss) regarding personal life
8. Has been made to feel embarrassed by a group of colleagues joking or sniggering about sexual conduct

At the workplace, sexual harassment can be broadly classified into two categories. The 'quid pro quo' type includes asking for sexual favours in exchange for work benefits and threatening the victim with dismissal or impossible/stressful working conditions in case of non-cooperation. The 'Hostile working environment' type of harassment refers to the creation of a hostile working atmosphere for the female employees to function in. This would include unwelcome activities like displaying of pornography or obscene graffiti, physical contact or brushing against female employees, and so on.

In India, the Vishaka guidelines provide a framework that emphasizes on prevention of sexual harassment and facilitates the adoption of preventive measures. These guidelines apply to women employed in both the organized and unorganized sectors and also to all women whether working full time or part time, on contract or in a voluntary capacity. As is expected, the guidelines stress on the adoption of a sexual harassment policy prohibiting sexual harassment at the workplace and providing well-thoughtout grievance procedures for all employees irrespective of their level in the organization.

In most developed countries, it is considered a crime to discriminate against any person seeking employment, on the basis of his/her sex. Hiring, terminating or promoting a person merely on the basis of the person's sex can result in legal intervention.

In the developed nations, laws have been enforced that require equal pay to be given to both men and women for equal work. Compensation discrimination based on the sex of the worker is also prohibited. However, the truth is that despite such laws, discrimination at work is a malady that refuses to be cured.

Sexual Harassment of Women at Workplace and Constitutional Guidelines and Norms

The three Judge Bench of the Supreme Court in *Vishaka* vs. *Union of India* in an epoch-making judgement made a significant contribution in evolving the code against sexual harassment. While emphasizing the need to have guidelines, the Supreme Court said that:

The legislature and the executive have the primary responsibility to ensure the safety and dignity of womencreating the right legislations and also building mechanisms for their enforcement. However, when instances of sexual harassment that have resulted in violation of fundamental rights of women workers under Articles 14, 19 and 21 are brought before us for redressal under Article 32, an effective redressal requires that some guidelines should be laid down for the protection of these rights to fill the legislative vacuum.

Guidelines and norms

For the enforcement and preservation of the right to gender equality of the working women, the Supreme Court of India has laid down norms and guidelines that are to be strictly observed at all workplaces. According to the Supreme Court, these directions are enforceable and binding in law until suitable legislation is enacted to occupy the field. However, these guidelines shall not prejudice any of the rights available under the Protection of Human Rights Act, 1993.

1. **Duty of the employer or other responsible persons in workplaces and other institutions.** It shall be the duty of responsible persons or the employer in institutions and workplaces to take the required and necessary steps for prevention of acts of sexual harassment, for determent

of the commission of sexual harassment acts, and provide the procedure for the settlement, resolution, and prosecution of sexual harassment acts.

2. **Preventive steps.** All persons in charge of the workplace or employers , be it in the private or public sector, should take suitable steps for prevention of sexual harassment. The following steps are required to be taken by them:

   (*i*) At the workplace prohibition of sexual harassment, as described above, should be published, notified, and circulated in suitable ways.

   (*ii*) The rules and regulations relating to conduct and discipline of the public sector and government bodies should include rules and regulations that help in prohibiting sexual harassment and also provide the right penalties against the offender.

   (*iii*) As regards the employers in the private sector, steps should be taken by them for inclusion of the aforesaid prohibitions in the standing orders of their company, under the Industrial Employment (Standing Orders) Act, 1946.

   (*iv*) To further guarantee that there is friendly environment towards women at the workplace, appropriate work conditions should be provided in respect of health, work, leisure and hygiene and no woman employee should have reasonable grounds to believe that she is disadvantaged in her current employment.

3. **Disciplinary action.** The employer should initiate disciplinary action in accordance with the rules, where the conduct of the accused amounts to misconduct in employment under the relevant service rules.

4. **Complaint mechanism.** For the redressal of the complaint made by the victim, the employer is required to create an appropriate complaint mechanism in his organization to decide whether or not the conduct of the accused constitutes a breach of service or an offence under law. The time-bound disposal of complaints should be ensured by such a complaint mechanism.

5. **Complaint committee**

   (*a*) ***Design of complaint mechanism:*** The complaint mechanism should be adequate to provide where necessary a complaint committee, a special counsellor, or other support service (including maintenance of confidentiality).

   (*b*) ***Composition of complaint committee:*** The composition of the complaint committee shall be as under:

      (*i*) It shall be headed by a woman.

      (*ii*) Not less than half of its members of the committee be women.

      (*iii*) The committee should involve a third party, either an NGO or another body familiar with the issues of sexual harassment, in order to prevent the possibility of any undue pressures or influence from the senior levels.

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1. Define sexual harassment.
2. Mention one way in which unethical sales campaigns can affect women.
3. What is corruption?
4. How can corruption endanger lives?

(*c*) ***Annual report:*** The complaint committee of the concerned government department shall prepare an annual report of its activities of the previous year. Such report should also state complaints and actions taken by them. The committee shall forward a copy thereof to the head of the organization concerned who shall forward the same to the government department concerned with its comments.

(*d*) ***Compliance report:*** The employer and the person in charge is also required to report:

(*i*) On compliance with the aforesaid guidelines.

(*ii*) Compliance on the reports of the complaint committee.

(*iii*) Such report must be sent to the concerned government department.

6. **Workers' initiative.** In order to prevent and control sexual harassment at the workplace, employers should be allowed to raise these issues:

   (*i*) At workers' meetings
   (*ii*) In other appropriate forums

   The issues of sexual harassment should be affirmatively discussed in employer–employee meetings.

7. **Awareness.** In order to create awareness about the right of female employees in regard to sexual harassment, the employer should take the following steps: (*i*) prominently notify the guidelines in a suitable manner; and (*ii*) enact appropriate legislation on the subject, and also be suitably notified and displayed.

8. **Third party harassment.** Where sexual harassment occurs as a result of an act or omission by (*i*) any third party or (*ii*) outsider, the employer and persons in charge are required to take necessary and reasonable steps to assist the affected person (*a*) in terms of support; and (*b*) take preventive action.

9. **Steps to be taken by the government.** The Central and state governments are required to:

   (*i*) Take suitable measures (including legislation)
   (*ii*) Ensure that the guidelines are observed by the employers in private sector

Two years later, in *Export Promotion Council* vs. *A. K. Chopra*, the Supreme Court was invited to decide the following issues:

1. Does an action of the superior against a female employee, which is against moral sanctions and does not withstand the test of decency and modesty not amount to sexual harassment?
2. Is physical contact with the female employee an essential ingredient of such a charge?
3. Does the allegation that the superior 'tried to molest' a female employee at the 'place of work' not constitute an act unbecoming of good conduct and behaviour expected from the superior?

The Supreme Court's response on the aforesaid issues was as follows:

With regards to the first issue, the Supreme Court ruled that 'each incident of sexual harassment at the place of work results in violation of: the fundamental right to life and liberty and the right to gender equality —the two most precious fundamental rights guaranteed by the Constitution of India'.

The Supreme Court answered the second issue in negative and ruled that it was not correct to hold that since the respondent had not 'actually molested' Miss X and that he had only 'tried to molest' her and had 'not managed' to make physical contact with her, the punishment of removal from service was not justified.

5.6 SUMMARY

Corruption, environment ethics, gender ethics and sexual harassment or discrimination are all issues that have been animatedly discussed at seminars and conferences all over the world. However, very little of what is preached is brought into practice. It is clear that while the developed nations continue to progress, the state of the women, especially in the third world countries, continues to fall and the degree of corruption continues to rise.

5.7 ANSWERS TO 'CHECK YOUR PROGRESS'

1. According to the Supreme Court, sexual harassment is any unwelcome sexually-determined behaviour that includes physical contact, a demand or request for sexual favours, sexually-coloured remarks, showing pornography, any other physical, verbal or non-verbal conduct of a sexual nature.
2. In the Third World countries, often aggressive and unethical sales campaigns lead illiterate women to believe that breastfeeding is no longer the best way to feed an infant. With declining breastfeeding rates, the state of health of women and children have been far from enviable.
3. Corruption refers to the abuse of public office, that is, use of public office for some personal benefit.
4. Corruption, many a time, can be a matter of life and death. For example, corruption in the pharmaceutical industry, resulting in spurious drugs flooding the market, may mean the death of many innocent people.

5.8 EXERCISES AND QUESTIONS

1. Globalization has actually heightened gender inequality. Discuss.
2. Sexual harassment is a major concern in India. Discuss.

5.9 FURTHER READING

Modh, Satish, *Ethical Management: Text and Cases in Business Ethics and Corporate Governance.* New Delhi: Macmillan Publishers India Ltd, 2005.

Mathur, U.C., *Corporate Governance and Business Ethics: Text and Cases.* New Delhi: Macmillan Publishers India Ltd, 2005.

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