ETHICAL BEHAVIOUR AND CORPORATE GOVERNANCE

PRESENTATION BY
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TO THE INSTITUTE OF CHARTERED ACCOUNTANTS GHANA
June 2, 2011 at Koforidua
I. Structure of Presentation

• Introduction
• Factors in economic growth and development
• Defining corporate governance
• Evolution of corporate governance
• Key points to note
• Significance of corporate governance
• Models of corporate governance
• Framework for corporate governance of businesses in Ghana
• Ethical perspectives of corporate governance
• Conclusion: The Future of Corporate Governance in Ghana
II. Factors in Economic Growth and Development

Three factors:
• Human capital
• Physical capital
• Technology

Emergence of a fourth factor:
• Institutions- Ensures efficient use of the three key factors

“Institutions are the rules of the game in a society or more formally, are the humanly devised constraints that shape human interaction” (Douglas North, 1990- Nobel Laureate)

Corporate governance is an institution in the above sense and is also a fundamental necessity for ensuring the efficient development of the three key factors of economic growth
Factors in Economic Growth and Development

Human Capital

Physical Capital

Technology

Economic Growth

Corporate Governance
III. Defining Corporate Governance

• Cadbury:

The system by which companies are directed and controlled. *(describes how companies ought to be run, directed and controlled.)*

• Kyereboah-Coleman and Biekpe:

It is about supervising and holding to account those who direct and control the management. *(embodies legitimate lines of accountability by defining the nature of the relationship between the company and key corporate constituencies.)*
Contd. Defining Corporate Governance

• **Deakin & Hughes**:  
  Relationship between the internal governance mechanisms of corporations and society’s conception of the scope of corporate accountability.

• **Keasey et al**:  
  The structures, processes, cultures and systems that engender the successful operation of organizations.

• **Maati**:  
  The whole set of measures taken within the social entity, i.e. the enterprise, to favour the economic agents to take part in the productive process in order to generate some organisational surplus, and to set up a fair distribution between the partners, taking into consideration what they have brought to the organisation.
Defining Corporate Governance

• **OECD:**

The system by which business corporations are directed and controlled. The Corporate Governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders and spells out the rules and procedures for making decisions in corporate affairs. By doing this, it also provides the structure by which the company objectives are set and the means of attaining those objectives and monitoring performance.
IV. Evolution of Corporate Governance

• Emerged with the formation of joint-stock companies and democratic capitalism (share ownership)

• ** Principal-Agent Paradigm  
  – Fundamental agency problem: Berle & Meane (1932)
  – Agency theory: Jensen and Meckling (1976)

• ** Principal faces 2 main problems:**
  – Selection of most capable managers
  – Giving managers the right incentives to put forth appropriate efforts and make decisions aligned with shareholders’ interests
• Corporate failures of recent times
  
  **internationally:**
  – Freddie Mac and Fannie Mae
  – Enron
  – Barings Bank
  – Royal Bank of Scotland
  – Northern Rock
  – WorldCom
  – Merril Lynch
  – Anderson

  **in Ghana:**
  – Meridian BIAO
  – Bank for Housing and Construction
  – Cooperative Bank
V. KEY POINTS TO NOTE

- Shareholders and other stakeholders
- Fairness
- Transparency
- Accountability
- Legal and Regulatory Framework
- Risk Management
- Information Flows
- Responsibility of Management and the Board
- Monitoring of actors
- CEO selection
- Executive compensation
VI. Significance of Corporate Governance

- Corruption
- Capital Markets
- Profitability
- Corporate Social Responsibility
- Bail-out by governments (implications for taxpayers)
- Capital Formation and Economic Growth
VII. Models of Corporate Governance

- **Shareholder Model**
  - Maximisation of wealth for investors and shareholders
  - Developing and improving the formal system of performance, accountability between management and shareholders
  - Making decisions based on what is best for investors

- **Stakeholder Model**
  - Corporate social responsibility
  - Considers the interest of employees, suppliers, government agencies, communities and groups with which it interacts
  - Assumes a collaborative and relational approach to business

- **Triple Bottom Line Model**
  - Economic, social, environmental

General push is for the stakeholder or corporate responsibility model by companies worldwide. This embraces the Shareholder Model.
VIII. Corporate Governance Framework in Ghana

• The Companies’ Code, 1963 (Act 179)
  – All registered corporate entities

• The Securities Industry Law, 1993 (PNDCL 333) and The Securities Industry (Amendment) Act, 2000 (Act 590)
  – Regulating stock exchanges, investment advisors, securities dealers, collective investment schemes which are licensed under the Securities & Exchange Commission
Corporate Governance Framework in Ghana

• The Ghana Stock Exchange’s Listing Regulations, 1990 (L.I.1590) Rules on Takeovers & Mergers
  - Regulating listed companies

• Bank of Ghana Regulations
  – Regulating banks and other Financial Institutions

• National Insurance Commission
  – Regulating insurance companies and insurance brokers
The above legal framework contains provisions which are relevant for effective Corporate Governance:

• **Board of Directors**
  – The business of the Company is managed by the Board, except where the Regulations of the Company prescribe otherwise. The relevant issues are: membership, independence and expertise.
  – Shareholders appoint directors
  – Membership qualifications ensure that people of integrity are appointed
  – Minimum of 2 directors, maximum to be fixed by each company.
contd.

Corporate Governance Framework in Ghana

– No requirement to appoint independent directors
– The Code allows the appointment of Executive Directors. No prescription for a balance exists.
– Different shareholders interests may be represented.
– CEO duality: the Code does not provide for separation of CEO and Board Chairman.
– Fiduciary role of Directors
– Provides sanctions in the event of breaches
Corporate Governance Framework in Ghana

• **Tripartite Audit Functions**
  – Internal Audit
  – External Audit
  – Audit committee of the Board

• **Audit Committees of the Board**
  - Not a requirement under the Code
  - Required under GSE and BOG Rules
  - Good practice
contd.

Corporate Governance Framework in Ghana

- Terms of Reference of Audit Committees
  - To monitor the integrity of financial statements of companies and any formal announcement relating to the company’s financial performance
  - Reviewing the company’s internal financial and other controls
  - To monitor and review the effectiveness of the company’s internal and external audit functions

• Quality Control in the Auditing Process and application of Ethical standards

• Mandatory Rotation of external auditors-BoG sets the pace
contd.

Corporate Governance Framework in Ghana

• **Financial Reporting & Disclosures**
  – Reporting Standards - IFRS
  – Mandatory Disclosures
  – Voluntary Disclosures
  – Reporting should be timely and integrity-driven
  – Adequacy of Disclosures to Stakeholders???
    • Investigating Stakeholder information needs
    • IFRS and legal requirements being minimum
    • Enforcement of mandatory disclosures- Trends in Ghana?
    • Voluntary disclosures may be necessary to ensure more balanced reporting
      ✓ Value-added statements
      ✓ Environmental Reporting
      ✓ Other non-financial reporting
Disclosure choices are cost-benefit issues (paradoxical)- ethical conduct is necessary here!

**Risk Management**

- Types of Risks
  - Reputation risk
  - Financial risk
  - Physical risk
  - Credit risk
  - Operational risk
  - Other risks???

- Focus on Risks to ensure a stable organization and avoid any upheavals
- Effective internal controls and related monitoring required
contd. Corporate Governance Framework in Ghana

- **Monitoring**
  - Board should ensure that good practices are implemented
  - Board should carry out self-assessment exercises
  - External regulators, i.e. Registrar of Companies, SEC, BOG, GSE, NIC, ICAG, should perform their roles
IX. Ethical Perspective of Corporate Governance

Definition of Ethics:

Ethics may be defined as a system of moral principles. It may also be viewed as a branch of philosophy dealing with right and wrong and the morality of motives and ethos.

Moral principles differ from person to person so are the notion of what is right or wrong, belief systems and motives.

What then is ethical behaviour? (If I may ask) It appears to me that it is a personal definition – knowledge of which helps define the choices we make, the goals we attain and the path our lives navigate.
Ethical Perspective of Corporate Governance

Our ethical portfolio is shaped by our EVERYTHING: experiences, peers, religious beliefs, edicts from a power we deem higher than ourselves (e.g. International laws, Ayatollah, Pope, Supreme Consciousness), people to whom we are exposed and even our decision to seek out models of ethical behaviour.

Dr. Elmer Hess, President of the American Medical Association, has observed:

“If a man is good in his heart, then he is an ethical member of any group in society. If he is bad in his heart, he is an unethical member”.

He adds that to him,

“the ethics of medical practice is as simple as that”.
Ethical Perspective of Corporate Governance

• Ethics is concerned with what we are and not just what we do. It is obedience to the unenforceable

• Four Cardinal Virtues for Ethical Behaviour
  • Prudence – good judgment, competence, practical reasoning
  • Justice (fairness)
  • Courage (fortitude) – not foolhardiness or recklessness
  • Self-mastery – discipline or temperance

• Trust, integrity, fairness matter and are crucial to the bottom line.
Ethical Perspective of Corporate Governance

• **Adequacy of Legal Compliance**
  – proven to be inadequate.
  – lacks the moral firepower to restore confidence and build trust
  – Many abuses in the past were entirely legal
  – Diminished capacity of the uninformed in understanding sophisticated models e.g. derivatives
  – Well-counselled executives have many tricks

• **Ethical Dimensions**
  – Relationships and Building trust (in and outside the organization)
  – Concerned with reasons, motives, intentions
  – Embraces the letter and spirit of regulations
Ethical Perspective of Corporate Governance

Board’s Role in Ethical Leadership:

• Should make ethical standards part of the corporate agenda

• Have broad ethical awareness

• Lead in setting ethical standards

• Ensure enforcement of ethical behaviour

• Build commitment and respect for values

• Meet social obligations

• Train employees, management and the board in best business practices
X. CONCLUSION

Future of Corporate Governance in Ghana

- Embrace Stakeholder Model
- Ethical Leadership Principles and expectations
- Strengthen disclosure practices; enforce mandatory fully and encourage voluntary disclosures
- Develop company purpose statements that cover stakeholder interests
- Implement Board self-assessment
- Rigorous board membership requirements
- Requisite competencies in board composition
- Ask tough questions about controversial issues and embrace objectivity
- Strengthen capacity of regulatory agencies
- Review the companies’ code to strengthen its corporate governance credentials
- Debate on executive compensation
References