

## **Paper 6- Laws, Ethics and Governance**

**Paper 6- Laws, Ethics and Governance**

Full Marks:100

Time allowed: 3 hours

**Section A**

1. Answer the following questions

[20 × 1 = 20]

(a) Multiple choice questions:

(i)	(a)	Coercion
(ii)	(c)	Tacit Contract
(iii)	(a)	a implied condition as to be description of goods
(iv)	(c)	Who has completed 15 years but less than 18 years
(v)	(b)	100 or more workers
(vi)	(b)	before the expiry of 10th day of the following month
(vii)	(b)	4.75% and 1.75% of wages respectively
(viii)	(c)	20 or more persons
(ix)	(c)	No child shall be permitted to work in any establishment on any day which he has already been working in another establishment.
(x)	(a)	Vernacular
(xi)	(d)	Share Certificate
(xii)	(d)	All of the above
(xiii)	(c)	60 days
(xiv)	(d)	1 <sup>st</sup> July 2005
(xv)	(b)	Red-herring prospectus
(xvi)	(c)	48 hours from the date of receipt of request
(xvii)	(a)	is not less than 21 years of age
(xviii)	(b)	two-tier concept
(xix)	(c)	Principles or standards
(xx)	(b)	Compliance, Contribution and Consequences

(b) Match the following:

[5 × 1 = 5]

1. D
2. A
3. E
4. B
5. C

2. Answer any three questions:

[3 × 15 = 45]

(a) (i) Distinction between Contract of Indemnity & Contract of Guarantee:

The differences between contract of guarantee and contract of indemnity is as follows:

S. N.	Contract of Indemnity	Contract of Guarantee
1.	There are two parties to a contract, indemnifier and indemnified.	There are three parties to contract, creditor, principal debtor and surety.
2.	The liability of the indemnifier is primary and independent	The liability of the surety is secondary and collateral, the principal debtor being primarily liable.

## Answer to MTP\_Intermediate\_Syllabus 2012\_June2016\_Set 2

3.	The number of contract is one, between indemnifier and indemnified.	The number of contract is three, (a) between principal debtor and creditor (b) between creditor and surety (c) between surety and principal debtor.
4.	The liability of the indemnifier is subject to happening of a contingency.	There is an existing debt the performance of which is guaranteed by the surety.
5.	The indemnifier need not act only at the request of the indemnified.	The surety should give guarantee only at the request of the principal debtor.
6.	The indemnifier cannot proceed against third parties in his own name unless there is an assignment in his favour.	After discharging the debt the surety can proceed against the principal debtor in his own name.

(ii) The seller who has not received the whole of the price of the goods sold is called an "unpaid seller". According to Section 45, the seller of goods is deemed to be an unpaid seller:

- (a) When the whole of the price has not been paid, or
- (b) When a bill of exchange or other negotiable instrument has been received as conditional payment, and the same has been dishonoured.

A seller who has been partly paid is also an unpaid seller.

### **Rights of an unpaid seller:**

According to the Sale of Goods Act the unpaid seller has the following rights. They are:

- A. Rights against the goods
- B. Rights against the buyer

#### **A. Rights against the goods:**

An unpaid seller has some rights against the goods sold when the property in the goods has passed to the buyer. They are as follows:

- (1) Right of Lien
- (2) Right of stoppage of goods in transit
- (3) Right of Re-sale
- (4) Right of withholding delivery

#### **1. Right of Lien: [Sec. 47]**

Lien is a right to retain possession of goods until payment of price. According to section 47(1) an unpaid seller can exercise the right of lien in the following cases:

- (i) Where the goods have been sold without any stipulation as to credit.
- (ii) Where the goods have been sold on credit, but the period of credit has expired.
- (iii) Where the buyer becomes insolvent.

#### **2. Right of stoppage of goods in transit: [Sec. 50]**

The right of stoppage in transit is a right of stopping the goods, while they are in transit and retaining the possession until payment of the price. This right is conferred on the seller by Section 50 of the Act. This right can be exercised under the following cases:

- (i) the seller must be an unpaid seller.
- (ii) the goods must be in-transit
- (iii) the buyer must have become insolvent.
- (iv) the property in the goods must have passed from the seller to the buyer.

#### **3. Right of Re-sale: [Sec. 54]**

An unpaid seller who has exercised either the right of lien or the right of stoppage-in-transit can resell such goods. The right to resell the goods is called 'right of resale'. This right is conferred by section 54. An unpaid seller can exercise the right of resale in the following cases:

- (i) where the goods are of a perishable nature,
- (ii) where the seller expressly reserves the right of resale in case the buyer makes a default in the payment of price.
- (iii) where the seller has exercised his right of lien or stoppage in transit, and gives notice to the buyer of his intention to resell the goods.

### **B. Rights against the buyer personally:**

An unpaid seller in addition to his rights against the goods, has the following rights against the buyer personally.

#### **1. Suit for price: [Sec. 55]**

Where the property in goods has passed to the buyer, and the buyer wrongfully neglects or refuses to pay the price, the seller can sue the buyer for price.

#### **2. Suit for damages for non-acceptance: [Sec. 56]**

Where the buyer wrongfully neglects or refuses to accept and pay for the goods, the seller can sue him for damages for non-acceptance of the goods.

#### **3. Suit for repudiation:**

Where the buyer repudiates the contract before the date of delivery, the seller may wait till the date of delivery or may treat the contract as cancelled and sue for damages for breach.

#### **4. Suit for interest: [Sec. 61]**

Where there is specific agreement between the seller and the buyer regarding interest on the price of goods, the seller may claim it from the date when payment becomes due. If there is no specific agreement, the interest is payable from the date notified by the seller to the buyer.

### **(b) (i) Eligibility for bonus:**

Following conditions should be satisfied for entitlement of bonus under Payment of Bonus Act:

- (i) he was worked not less than 30 days
- (ii) his salary / wage does not exceed ₹ 21,000 per month.
- (iii) Provided such establishment comes under the payment of Bonus Act.

#### **Disqualification for bonus: (Sec. 9)**

Notwithstanding contained in the Act, an employee shall be disqualified from receiving bonus under the Act, if he is dismissed from services for:

- (a) Fraud;
- (b) Riotous or violent behavior while on the premises of the establishment; or
- (c) Theft, misappropriation or sabotage of any property of the establishment.

If an employee is illegally terminated from service, he still remains qualified and eligible to receive bonus. Where an employee was prevented from working by reason of an illegal order, he would be eligible for bonus.

### **(ii) Employer to pay compensation:**

In case a personal injury is caused to a workman by accident arising out of and in the course of employment, his employer is liable to pay compensation in accordance with the provisions of the Act within 30 days from the date when it fell due otherwise he would also be liable to pay interest and penalty.

#### **When employer is not liable to pay compensation:**

The Compensation payable under the Act is to be made by deposit to the Commissioner of Employee's Compensation who will distribute the same to Employee or his dependents. However, amount equal to 3 months wages can be paid directly to the dependents in cases of death of Employee, provided the said amount is less than the total compensation payable to Employee. Report of death and serious bodily injury should be given within 7 days of the death/serious bodily injury to the Commissioner of Employee's Compensation.

**(c) (i) Difference between Negotiation and Assignment:**

Negotiation	Assignment
1. Negotiation may be effected by mere delivery if the instrument is bearer one or endorsement and delivery if it is an order instrument.	1. Assignment should always be on a written document signed by transferor.
2. Transferee gets the title of Holder in due course.	2. Title of the transferee is always subject to the title of the transferor.
3. Consideration is always presumed.	3. Consideration must be proved.
4. No information of transfer needs to be given to the debtor in order to bind him.	4. Notice of assignment is must in order to bind the debtor.

**(ii) Meaning of Endorsement:**

**Sec. 15 of the Negotiable Instruments Act, 1881 defines 'Indorsement'.**

Sec. 15 Indorsement - When the maker or holder of a negotiable instrument signs the same, otherwise than as such maker, for the purpose of negotiation, on the back or face thereof or on a slip of paper annexed thereto, or so signs for the same purpose a stamped paper intended to be completed as a negotiable instrument, he is said to indorse the same, and is called the 'indorser'.

**Kinds of Endorsement:**

The following are the different kinds of endorsement:

1. Blank Endorsement. [Sec. 16]
2. Special Endorsement.
3. Restrictive Endorsement.
4. Conditional Endorsement.
5. Sans Recourse Endorsement.
6. Sans Frais Endorsement.
7. Facultative Endorsement.
8. Partial Endorsement.

**1. Blank Endorsement:**

**Section 16 of the Negotiable Instruments Act, 1881 explains about "Blank Endorsement".**

An indorsement is said to be blank when the indorser merely signs on the instrument, without mentioning the name of the person in whose favour the indorsement is made. In such a case, so long as the indorsement continues blank, the property in the negotiable instrument may be passed by mere delivery, exactly as if it were payable to bearer.

**2. Special Endorsement:**

When the indorsement contains not only the signature of the indorser, but also the name of the person in whose favour the indorsement is made, then that indorsement is said to in 'full or special'.

**3. Restrictive Endorsement:**

If an indorsement prohibits the further negotiation of a cheque or expresses that it is a mere authority to deal with the cheque as the indorsement directs and not a transfer of ownership of the cheque, it is known as "Restrictive Indorsement". If a restrictive indorsement does authorize further transfers, any subsequent indorsee must take the cheque subject to the restrictions imposed on the first indorsee under the restrictive indorsement.

**4. Conditional Endorsement:**

If an indorser indorses a cheque conditionally in favour of the indorsee, the indorsement is known as a "Conditional Indorsement". The indorser can make the indorsement in such a way that the right of the indorsee to receive the amount due thereon is made dependent upon the happening of a specified event, although such an event may never happen. The indorser is permitted to make the right of the indorsee to receive the payment contingent on the happening of some event or on the fulfillment of some condition.

5. **Sans Recourse Endorsement:**

"**Sans Recours**" means "**without recourse**" (to me). This endorsement limits the liability of the indorser. The effect of this indorsement is, to make the indorser free from all liability to any subsequent holder.

6. **Sans Frais Endorsement:**

"Sans Frais" means "without expense". In this kind of endorsement, the indorser does not want to incur any expenses on the instruments which may be charged by the bank. If his intention is indicated to the effect that he is not willing to bear any expenses means the payee, shall have to bear the expenses that may incur on the instruments. Under this indorsement the endorser is exempted from expenses of the instruments.

7. **Facultative Endorsement:**

Under this indorsement, the indorser waives some of his rights on the instrument. It is a general principle that when a bill is dishonoured, notice of dishonor should be served by the holder to all the previous parties. In this case, the holder can, without serving any notice to B, make him liable, in case the bill is dishonoured.

8. **Partial Endorsement:**

A partial endorsement is that endorsement by which a right to receive a part payment. **Sec. 56 Indorsement for part of sum due** - "No writing on a negotiable instrument is valid for the purpose of negotiation if such writing purports to transfer only a part of the amount appearing to be due on the instrument, but where such amount has been partly paid, a note to the effect may be indorsed on the instrument, which may then be negotiated for the balance".

(d) (i) Section 46 of the Act envisages following six social security benefits:-

(a) **Medical Benefit:** Full medical care is provided to an Insured person and his family members from the day he enters insurable employment. There is no ceiling on expenditure on the treatment of an Insured Person or his family member. Medical care is also provided to retired and permanently disabled insured persons and their spouses on payment of a token annual premium of ₹ 120/- .

(b) **Sickness Benefit (SB):** Sickness Benefit in the form of cash compensation at the rate of 70 per cent of wages is payable to insured workers during the periods of certified sickness for a maximum of 91 days in a year. In order to qualify for sickness benefit the insured worker is required to contribute for 78 days in a contribution period of 6 months.

1. **Extended Sickness Benefit (ESB):** SB extendable upto two years in the case of 34 malignant and long-term diseases at an enhanced rate of 80 per cent of wages.

2. **Enhanced Sickness Benefit:** Enhanced Sickness Benefit equal to full wage is payable to insured persons undergoing sterilization for 7 days/14 days for male and female workers respectively.

## Answer to MTP\_Intermediate\_Syllabus 2012\_June2016\_Set 2

---

(c) **Maternity Benefit (MB)** : Maternity Benefit for confinement/pregnancy is payable for three months, which is extendable by further one month on medical advice at the rate of full wage subject to contribution for 70 days in the preceding year.

(d) **Disablement Benefit**

1. **Temporary disablement benefit (TDB)**: From day one of entering insurable employment & irrespective of having paid any contribution in case of employment injury. Temporary Disablement Benefit at the rate of 90% of wage is payable so long as disability continues.
2. **Permanent disablement benefit (PDB)**: The benefit is paid at the rate of 90% of wage in the form of monthly payment depending upon the extent of loss of earning capacity as certified by a Medical Board.

(e) **Dependants' Benefit (DB)** : DB paid at the rate of 90% of wage in the form of monthly payment to the dependants of a deceased Insured person in cases where death occurs due to employment injury or occupational hazards.

(f) **Other Benefits:**

- **Funeral Expenses**: An amount of "10, 000/- is payable to the dependents or to the person who performs last rites from day one of entering insurable employment.
- **Confinement Expenses**: An Insured Women or an LP. in respect of his wife in case confinement occurs at a place where necessary medical facilities under ESI Scheme are not available.

(ii) The given problem is a case of "coercion" as according to section 15 of the Indian Contract Act, 1872 "coercion" includes any contract obtained by committing any act which is forbidden by the Indian Penal Code. However, the Indian Penal Code need not be in force at place where the coercion is employed and at the time when coercion is employed. Further, as per section 19, when consent to an agreement is obtained by coercion, the contract is voidable at the option of the party whose consent was obtained by coercion. So, "A" cannot succeed.

(e) (i) According to Section 11 of the Indian Contract Act, 1872 a person who is of the age of majority to the law to which he is subject is competent to enter into any contract. A person who has completed the age of 18 years is a major and otherwise he will be treated as minor. Thus, Ramesh who is a minor is incompetent to contract and any agreement with him is void. [Mohori Bibi Vs. Dharmodas Ghose 1903]. Section 68 of the Indian Contract Act, 1872 however, prescribes the liability of a minor for the supply of the things which are the necessaries of life to him. It says that though minor is not personally liable to pay the price of necessaries supplied to him or money lent for the purpose, the supplier or lender will be entitled to claim the money/price of goods or services which are necessaries suited to his condition of life provided that the minor has a property. The liability of minor is only to the extent of the minor's property. This type of contract is called a Quasi-contract and the right of the supplier/lender is based on the principle of equity. Thus, according to the above provision, Suresh will be entitled to recover the amount of loan given to Ramesh for payment of the college fees from the property of the Ramesh.

(ii) In case of food article, there is an implied condition that the item is fit for human consumption. One of the condition as to quality & fitness. Hence there was a breach of condition as to fitness and XYZ & CO. was liable to pay damages (Frost V Avlesbury Dairy Co. Ltd. 1905 1 KB 608.)



- (iii) Section 138 of the Negotiable Instruments Act, 1881 states that where any cheque drawn by a person on an account maintained by him with a banker for payment of any amount of money to another person from out of that account for the discharge, in whole or in part, of any debt or other liability, is returned by the bank unpaid either because of the amount of money standing to the credit of that account is insufficient to honour the cheque or that it exceeds the amount arranged to be paid from that account by an agreement made with that bank, such person shall be deemed to have committed an offence. Asking payee not to present the cheque or issuing 'Stop Payment' instructions to the Banker gets covered u/s 138. Hence P is deemed to have committed offence.

**3. Answer any one question:**

**[1 x 15 = 15]**

**(a) (i) Related Party Transactions [Sec. 188]**

- (1) Except with the consent of the Board of Directors given by a resolution at a meeting of the Board and subject to such conditions as may be prescribed, no company shall enter into any contract or arrangement with a related party with respect to—
- (a) sale, purchase or supply of any goods or materials;
  - (b) selling or otherwise disposing of, or buying, property of any kind;
  - (c) leasing of property of any kind;
  - (d) availing or rendering of any services;
  - (e) appointment of any agent for purchase or sale of goods, materials, services or property;
  - (f) such related party's appointment to any office or place of profit in the company, its subsidiary company or associate company; and
  - (g) underwriting the subscription of any securities or derivatives thereof, of the company.

Provided that no contract or arrangement, in the case of a company having a paid-up share capital of not less than such amount, or transactions not exceeding such sums, as may be prescribed, shall be entered into except with the prior approval of the company by a special resolution.

Provided further that no member of the company shall vote on such special resolution, to approve any contract or arrangement which may be entered into by the company, if such member is a related party.

Provided also that nothing in this sub-section shall apply to any transactions entered into by the company in its ordinary course of business other than transactions which are not on an arm's length basis.

Provided also that the requirement of passing the resolution under first proviso shall not be applicable for transactions entered into between a holding company and its wholly owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval.

**Explanation.—**

In this sub-section,—

- (a) the expression "office or place of profit" means any office or place—
- (i) where such office or place is held by a director, if the director holding it receives from the company anything by way of remuneration over and above the remuneration to which he is entitled as director, by way of salary, fee, commission, perquisites, any rent-free accommodation, or otherwise;
  - (ii) where such office or place is held by an individual other than a director or by any firm, private company or other body corporate, if the individual, firm,



## **Answer to MTP\_Intermediate\_Syllabus 2012\_June2016\_Set 2**

---

private company or body corporate holding it receives from the company anything by way of remuneration, salary, fee, commission, perquisites, any rent-free accommodation, or otherwise;

(b) the expression "arm's length transaction" means a transaction between two related parties that is conducted as if they were unrelated, so that there is no conflict of interest.

- (2) Every contract or arrangement entered into under sub-section (1) shall be referred to in the Board's report to the shareholders along with the justification for entering into such contract or arrangement
- (3) Where any contract or arrangement is entered into by a director or any other employee, without obtaining the consent of the Board or approval by a resolution in the general meeting under sub-section (1) and if it is not ratified by the Board or, as the case may be, by the shareholders at a meeting within three months from the date on which such contract or arrangement was entered into, such contract or arrangement shall be voidable at the option of the Board and if the contract or arrangement is with a related party to any director, or is authorised by any other director, the directors concerned shall indemnify the company against any loss incurred by it.
- (4) Without prejudice to anything contained in sub-section (3), it shall be open to the company to proceed against a director or any other employee who had entered into such contract or arrangement in contravention of the provisions of this section for recovery of any loss sustained by it as a result of such contract or arrangement.
- (5) Any director or any other employee of a company, who had entered into or authorised the contract or arrangement in violation of the provisions of this section shall,—
  - (i) in case of listed company, be punishable with imprisonment for a term which may extend to one year or with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees, or with both; and
  - (ii) in case of any other company, be punishable with fine which shall not be less than twenty-five thousand rupees but which may extend to five lakh rupees.

### **(ii) Powers of Board [Section 179]**

- (1) The Board of Directors of a company shall be entitled to exercise all such powers, and to do all such acts and things, as the company is authorised to exercise and do.

Provided that in exercising such power or doing such act or thing, the Board shall be subject to the provisions contained in that behalf in this Act, or in the memorandum or articles, or in any regulations not inconsistent therewith and duly made thereunder, including regulations made by the company in general meeting.

Provided further that the Board shall not exercise any power or do any act or thing which is directed or required, whether under this Act or by the memorandum or articles of the company or otherwise, to be exercised or done by the company in general meeting.
- (2) No regulation made by the company in general meeting shall invalidate any prior act of the Board which would have been valid if that regulation had not been made.
- (3) The Board of Directors of a company shall exercise the following powers on behalf of the company by means of resolutions passed at meetings of the Board, namely:—
  - (a) to make calls on shareholders in respect of money unpaid on their shares;

- (b) to authorise buy-back of securities under section 68;
- (c) to issue securities, including debentures, whether in or outside India;
- (d) to borrow monies;
- (e) to invest the funds of the company;
- (f) to grant loans or give guarantee or provide security in respect of loans;
- (g) to approve financial statement and the Board's report;
- (h) to diversify the business of the company;
- (i) to approve amalgamation, merger or reconstruction;
- (j) to take over a company or acquire a controlling or substantial stake in another company;
- (k) any other matter which may be prescribed.

Provided that the Board may, by a resolution passed at a meeting, delegate to any committee of directors, the managing director, the manager or any other principal officer of the company or in the case of a branch office of the company, the principal officer of the branch office, the powers specified in clauses (d) to (f) on such conditions as it may specify.

Provided further that the acceptance by a banking company in the ordinary course of its business of deposits of money from the public repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise, or the placing of monies on deposit by a banking company with another banking company on such conditions as the Board may prescribe, shall not be deemed to be a borrowing of monies or, as the case may be, a making of loans by a banking company within the meaning of this section.

- (4) Nothing in this section shall be deemed to affect the right of the company in general meeting to impose restrictions and conditions on the exercise by the Board of any of the powers specified in this section.

**(b) (i)** This is discussed under Section 12 of the RTI Act, 2005.

- (i) Central Information Commission to be constituted by the Central Government through a Gazette Notification.
- (ii) Commission includes one Chief Information Commissioner and not more than ten Central Information Commissioners, who will be appointed by the President of India.
- (iii) The general superintendence, direction and management of the affairs of the Central Information Commission shall vest in the Chief Information Commissioner assisted by the Central Information Commissioners.
- (iv) Commission shall have its Headquarters in Delhi. Other offices may be established in other parts of the country with the approval of the Central Government.
- (v) The Chief Information Commissioners and the Central Information Commissioners shall be person of eminence in public life with wide knowledge and experience in law, science and technology, social service, management, journalism, mass media or administration or governance.
- (vi) The Chief Information Commissioner or a Central Information Commissioners shall not be a Member of Parliament or Member of Legislature of any State or Union Territory, as the case may be, or hold any other office of profit or connected with any political party or carrying on any business or pursuing any profession.

**(ii)** The business structure in Germany is detailed in Wymeersch (1998) where he identifies the most used business types in various continental European states. In Germany, as far as the larger business entities are concerned, the business types tend to be either public (Aktiengesellschaft AG) or private companies limited by shares (Gesellschaft mit beschränkter Haftung, GmbH). However, he identifies a hybrid that is also used in Germany- specifically, a hybrid of the GmbH & Co. KG, combining the advantages of the unincorporated Kommanditgesellschaft and the limited liability of GmbH.

In Germany, as in many continental European countries and the UK, there is a trend away from individual share ownership. The most influential shareholders are financial and non-financial companies, and there are significant cross-holdings, which mean that when analysing share ownership and control in Germany, one needs to look also at the links between companies. Banks, and especially a few large banks, play a central role in German corporate governance with representation on the supervisory boards of companies and links with other companies. Charkham (1994) identifies a number of reasons as to why banks are influential in Germany. First, there is direct ownership of company shares by banks; second, German shareholders generally lodge their shares with banks authorized to carry out their voting instructions (deposited share voting rights, or DSVR); third, banks tend to lend for the long term and hence develop a longer term relationship with the company (relationship lending); fourth, banks offer a wide range of services that the company may find it useful to draw upon. Given these factors, banks tend to build up a longer term, deeper relationship with companies, and their expertise is welcomed on the supervisory boards, hence the German corporate governance system could be termed an 'insider' system.

The German Corporate Governance system is based around a dual board system, and essentially, the dual board system comprises a management board (Vorstand) and a supervisory board (Aufsichtsrat).

The management board is responsible for managing the enterprise. Its members are jointly accountable for the management of the enterprise and the chairman of the management board co-ordinates the work of the management board. On the other hand, the supervisory board appoints, supervises, and advises the members of the management board and is directly involved in decisions of fundamental importance to the enterprise. The chairman of the supervisory board co-ordinates the work of the supervisory board. The members of the supervisory board are elected by the shareholders in general meetings. The co-determination principle provides for compulsory employees representation. So, for firms or companies which have more than five hundred or two thousand employees in Germany, employees are also represented in the supervisory board which then comprises one-third employee representative or one-half employee representative respectively. The representatives elected by the shareholders and representatives of the employees are equally obliged to act in the enterprise's best interests.

The idea of employee representation on boards is not always seen as a good thing because the employee representatives on the supervisory board may hold back decisions being made that are in the best interests of the company as a whole but not necessarily in the best interests of the employees as a group. An example, would be where a company wishes to rationalize its operations and close a factory but the practicalities of trying to get such a decision approved by employee representatives on the supervisory board, and the repercussions of such a decision on labour relations, prove too great for the strategy to be made a reality.

### **Key characteristics influencing German corporate governance**

<b>Feature</b>	<b>Key characteristic</b>
Main business form	Public or private companies limited by shares
Predominant ownership structure	Financial and non-financial companies
Legal system	civil law
Board structure	dual
Important aspect	compulsory employee representation on supervisory board.

## Answer to MTP\_Intermediate\_Syllabus 2012\_June2016\_Set 2

---

The committee on corporate governance in Germany was chaired by Dr. Gerhard Cromme and is usually referred to as the Cromme Report or Cromme Code. The code harmonizes a wide variety of laws and regulations and contains recommendations and also suggestions for complying with international best practice on Corporate Governance.

#### 4. Answer any one question:

[1 x 15 = 15]

##### (a) (i) A. Employee Awareness:

It should be noted and ensured that employees are aware of their legal and ethical responsibilities. Organization should train and motivate employees toward ethical behavior. Top management should initiate steps in developing such an ethical environment.

##### B. Encouraging communication:

Ethical organization need to provide channels through which employees could communicate with concerned Managers, for reporting frauds, mismanagement or any other form of detrimental behavior.

##### C. Ensuring fair treatment to Whistle Blowers:

A person or an employee who reports fraud, mismanagement or any other detrimental practices to the concerned Managers is called Whistle Blower. Organization should ensure protection and fair treatment to Whistle Blowers to reduce fraud.

##### (ii) The fundamental principles of Ethical Behaviour are:

**A. Integrity:** The principle calls upon all accounting and finance professional adhere to honesty and firmness while discharging their respective professional duties:

- Avoid being involved in activities which would impair the goodwill of the organization.
- Communicate adverse as well as favorable information with those concerned.
- Refuse any favour which could influence his actions in a negative way.
- Refuse to get involved in any activity which would adversely affect objectivity.
- Avoid conflicts and advise related parties on imminent conflicts.

**B. Objectivity:** Communicate information fairly and objectively in a transparent manner.

**C. Confidentiality:** Accounting and financial management should refrain from disclosing confidential information acquired during their work. When such information is to be disclosed to their subordinates in course of their normal work, care should be taken that ultimate confidentiality is maintained. However, an organization must to submit information required under a legal obligation or statutory ruling.

**D. Professional competence:** Finance and accounting professionals need to update their professional skills from time to time. It has to be ensured that the client or employer receives competent professional services based upon current and contemporary developments in the related areas.

**E. Obedience to Rules:** Accounting and finance professionals should comply with relevant laws and regulations and avoid such actions which may result into discrediting the profession.

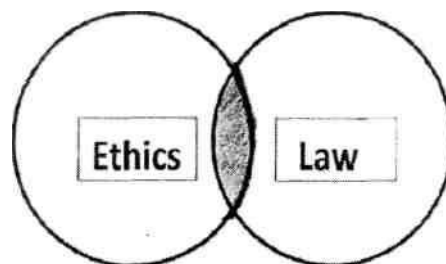
(b) (i) Ethical dilemma exists in all walks of business. Business situations are highly complex with no clear guidelines and equally justifiable alternatives. Hence, ethical dilemma should be dealt carefully. They arise when there are conflict in values with superiors in

the area of strategy, goals, policy and administration. Ethical issues get categorized in the following four main areas:

- (i) **Business Relationships:** i.e. relationships with customers, suppliers and others in the work place also have ethical concerns. Ethical behavior in the business involves meeting obligations and responsibilities duly on time, keeping company secrets and avoiding undue pressure that may force others to act unethically. The managers and other superiors can use their authority to influence the employees and make them act in an unethical manner. In the process, the manager may tell the employees to adopt unethical practices which the employee may not be willing to adopt. The ethical practices of the business must be focused on customer needs as the customer is the life line of the business. Organisations that cater to customer needs by adopting an honest and ethical approach make the customer feel that they are important and this in turn guarantees the success of the organization in the long run.
- (ii) **Conflict of interest:** Conflict of interest exists when a person has to decide whether to proceed with his own personal interest or in the interest of the organization. Example: Bribe is a conflict of interest because it benefits the individual but harms the organisation and the society. Conflict of interest can be managed in an effective manner when employees are able to separate either personal interests from their business dealings. Sam Walton, the late founder of Wal-Mart, banned company buyers from accepting even a cup of coffee from suppliers. It is not always necessary that conflict of interest should be financial.
- (iii) **Fairness and honesty:** Fairness and honesty are difficult principles of business ethics, which an organization is expected to follow. It is not enough for a company to ensure compliance with applicable laws and regulations, it should not cause any harm to employees, customers, competitors knowingly by means of unfair and deceptive trade practices. Disclosure of potential harm caused by product use is an example of "fairness and honesty". Though the legal system encourages competition and prevents monopoly, business organisations continue doing activities causing harm to the competition. Thus, ethical conduct of business depends on their Commitment to fairness and honesty.
- (iv) **Communication:** Organisations need to communicate with its environment to sustain and grow. They have to give true and correct information about their products and services. Nowadays, false and misleading advertisements occupy the business world. Consumers have a right to know full and true information about product's quality, price and safety. Manufacturers often fail to communicate the differences or similarities between products.

### (ii) Ethics and Law- The Interface

Law is essentially an institutionalization or codification of ethics into specific social rules, regulations and prescriptions. Perhaps the best way of visualizing ethics and law is in terms of two intersecting domains as depicted in the following figure:



Thus, in one sense, business ethics can be said to begin where law ends. Business Ethics is primarily concerned with those issues not completely covered by law, or where there is no definite consensus on whether something is right or wrong. Hence, it

## **Answer to MTP\_Intermediate\_Syllabus 2012\_June2016\_Set 2**

---

is often remarked, that business ethics is about the "grey areas" of business where values are in conflict.