



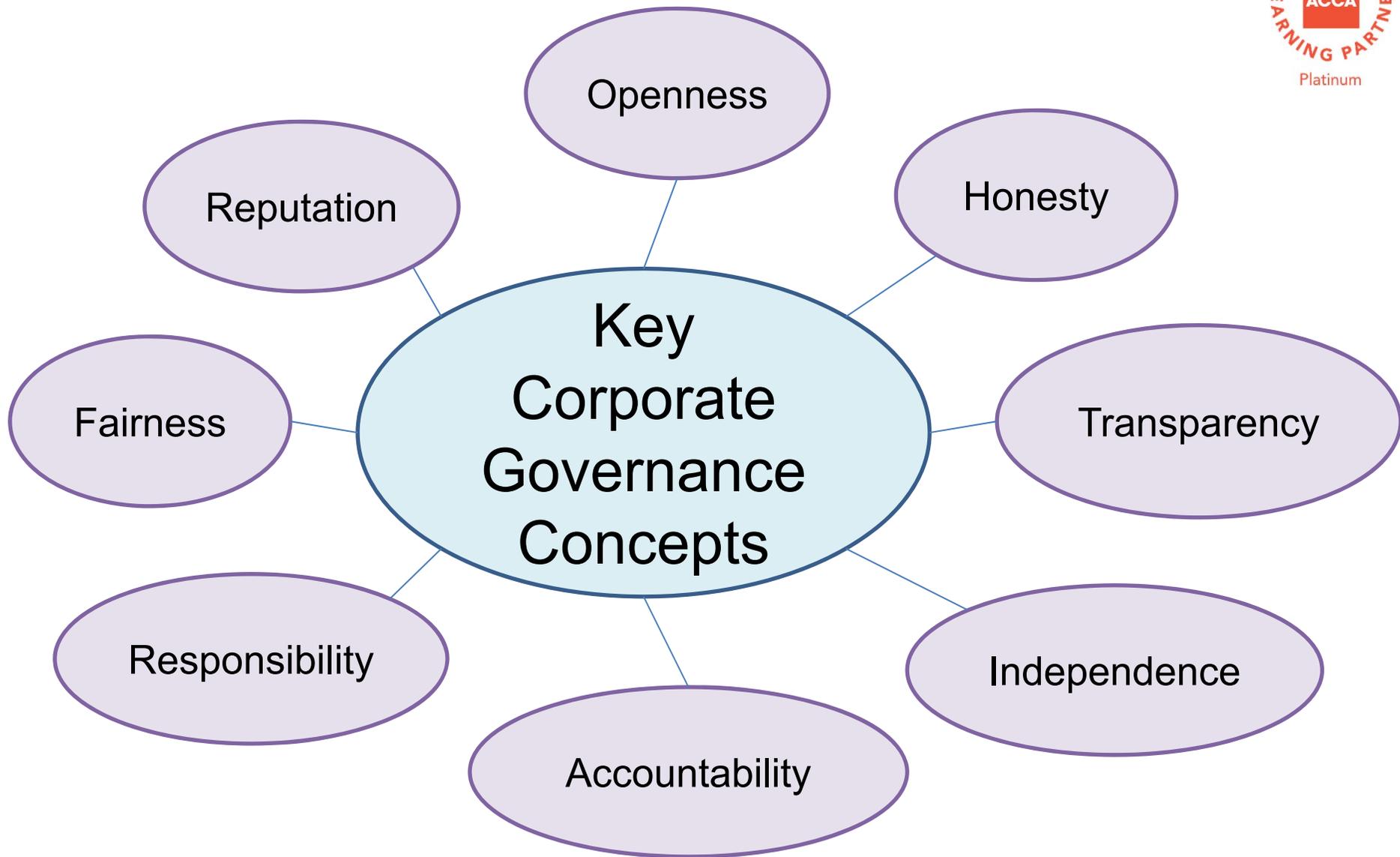
ACCA

P1 Governance, Risk & Ethics

Revision Classes

26 & 27 May 2017

Presented By: Goh Hong Lim



Openness



Demonstrated by Board Willingness to:

- **disclose information timely** to the shareholders
- **accept constructive criticism** from parties who are playing the monitoring role

Honesty



Requires the Board to exercise the **duty of loyalty** by **NOT**:

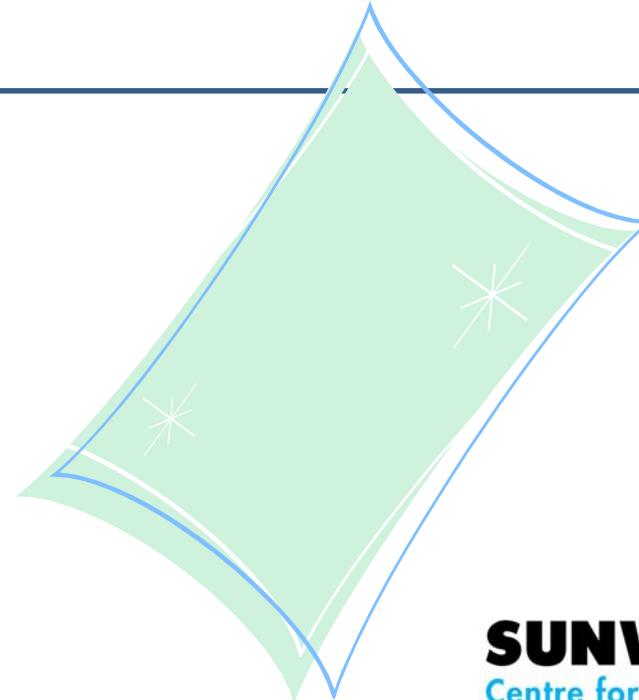
- **rewarding themselves** with **excessive remuneration**
- involving in **earning management** to deceive the shareholders

Transparency



This concept is characterised by:

- **timely disclosure** which are above the requirement
- the presence of **systems and procedures** to **govern decision making** which can curb malpractices



Independence



Applies to both **auditor and non-executive directors** who are playing the **monitoring role** in Corporate Governance.

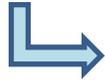
They are considered independent when they can be expected to express their **honest and professional opinion** in the best interest of the company.

Thus, their opinion should **avoid**:

- Biasness
- Conflict of interest
- Influence by others



Accountability



Requires the parties concerned to:

- **discharge their respective responsibilities** in accordance to the **role they hold** in corporate governance
- be **held responsible for the outcome of their decision**

There is **no accountability** if **one does not acknowledge** his or hers **responsibility towards another party**.

Responsibility



This concept is closely related to the accountability concept above. **Key issue** is to decide **who should have responsibility**.

Fairness



Requires **all shareholders** to be accorded **equal consideration** which means **minority shareholders** should be **treated** in the **same way** as majority shareholders.

Reputation



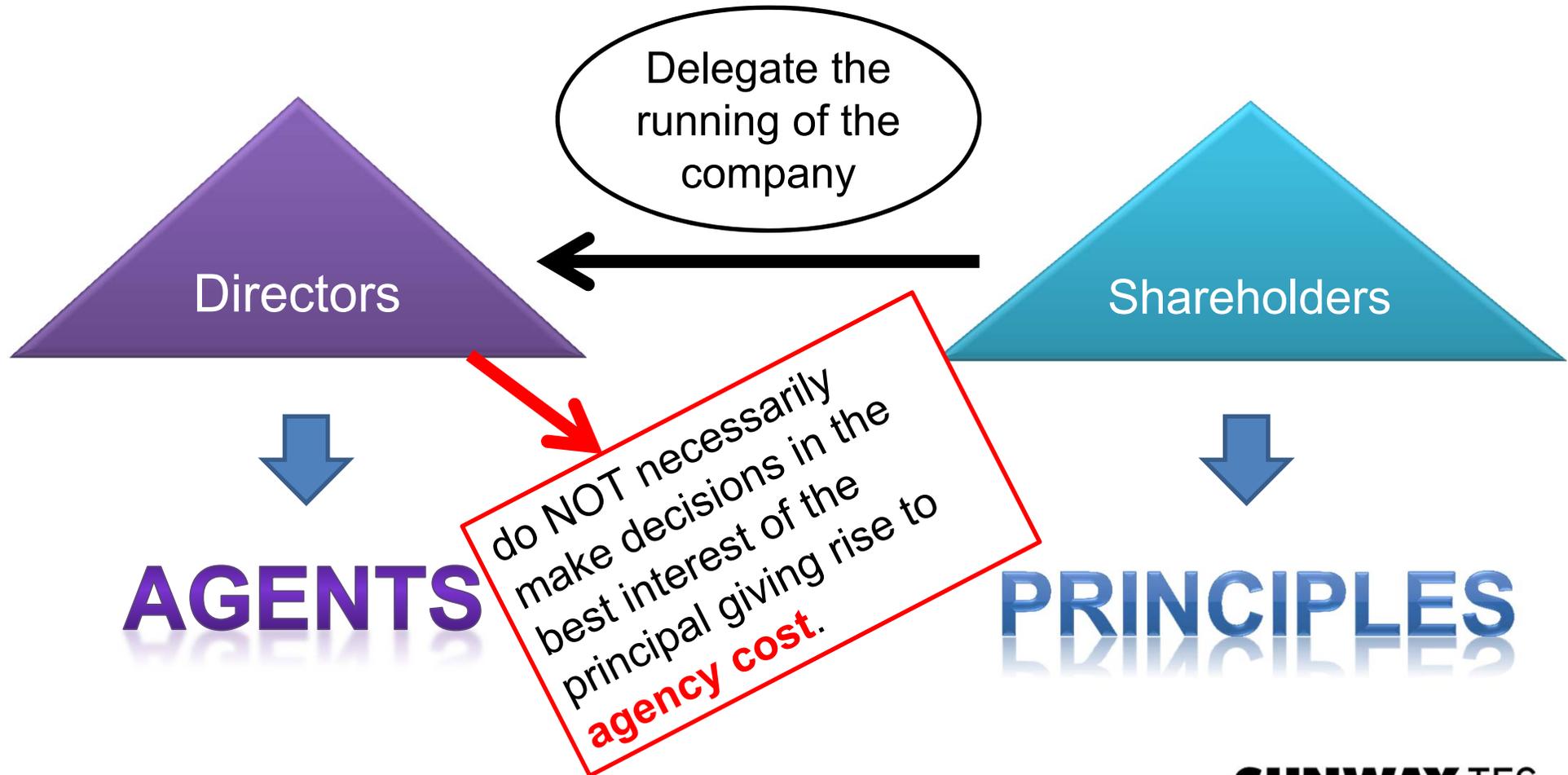
Company's **reputational risk** is **measured by** the **general deterioration of public perception** of:

- the company and
- the products or services it sells

Good Corporate Governance emphasises on **safeguarding a company's reputation** which is **akin to safeguarding the interest of shareholders**.

Agency Theory

Applicable for **larger sized companies** where the separation of ownership and control is the norm.



Agency Cost

Total agency cost comprise of:-

Sum of Principal
Monitoring
Expenditure



Fee payable to both the non-executive directors and the external auditors.



Time spent by the shareholders in attending the AGM and dialogues with management.

Agent's Bonding
Expenditure



Time spent by the directors in meeting with the institutional shareholders during the dialogues.

Residual Loss



Loss resulting from directors misusing their positions.

Solutions to agency problems



Incentives

The incentive solution ties an executive's wealth to the wealth of shareholders as that everyone shares the same goal.

Monitoring

The board of directors, auditors and other components of the governance system serve to monitor the executive management.

Fiduciary duty of directors



Fiduciary Given In Trust

Directors



Directors' role is similar to that of a trustee in a trust in that they are **entrusted** by the shareholders to run the company on their behalf.



Directors are expected to demonstrate:-



Uncompromising
loyalty to the
shareholders



To exercise due
diligence in
making decisions



Business cases associated with observing stakeholders' interest

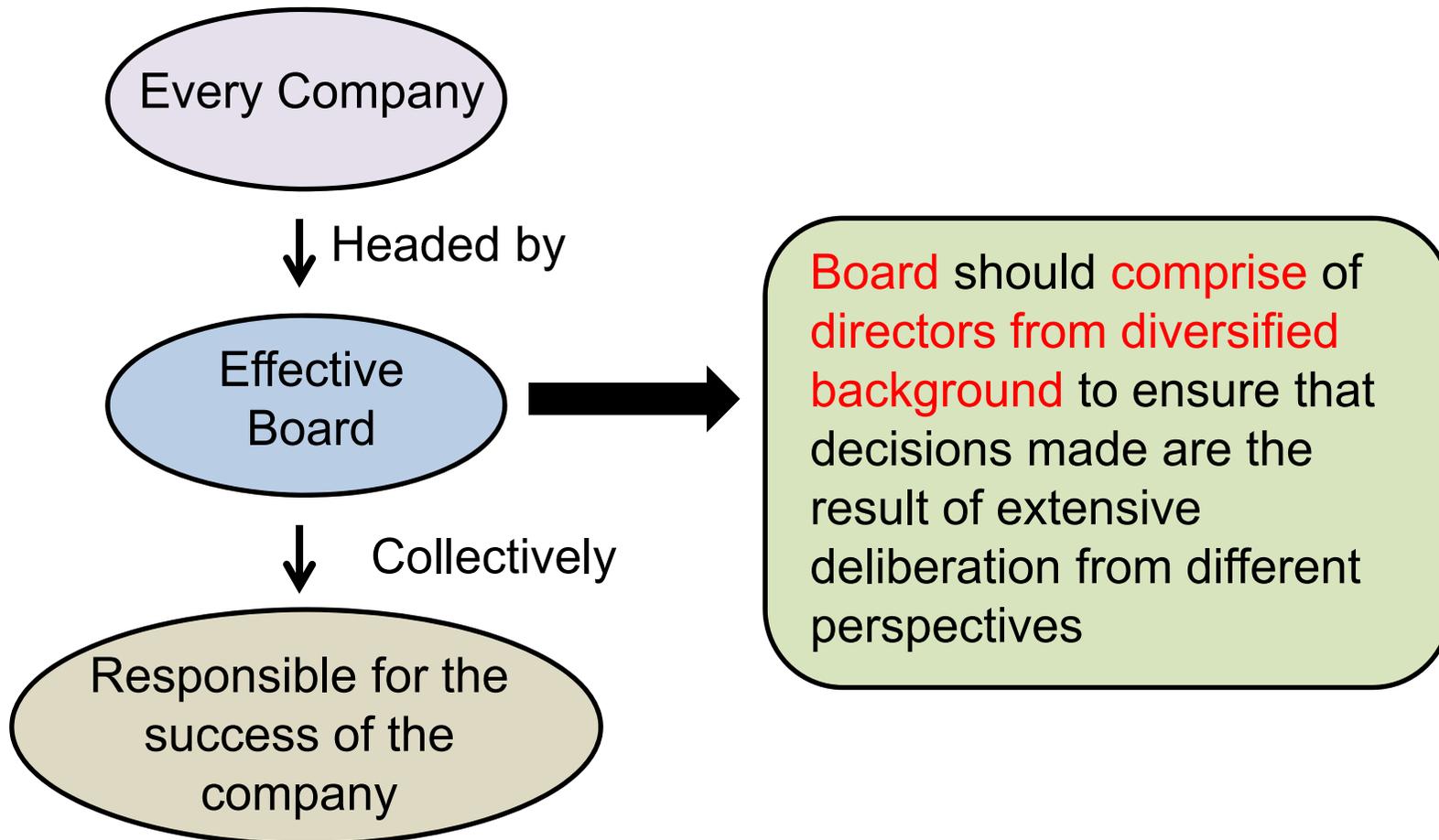
- Avoidance of negative action by non-governmental organisation against the company.
- Penetration of new markets that value ethical business practices.
- Attract and retain staff who share the same values as the company.
- Ease of raising finance possibly from ethical fund.
- Lower cost of capital due to perceived lower risk by financiers.



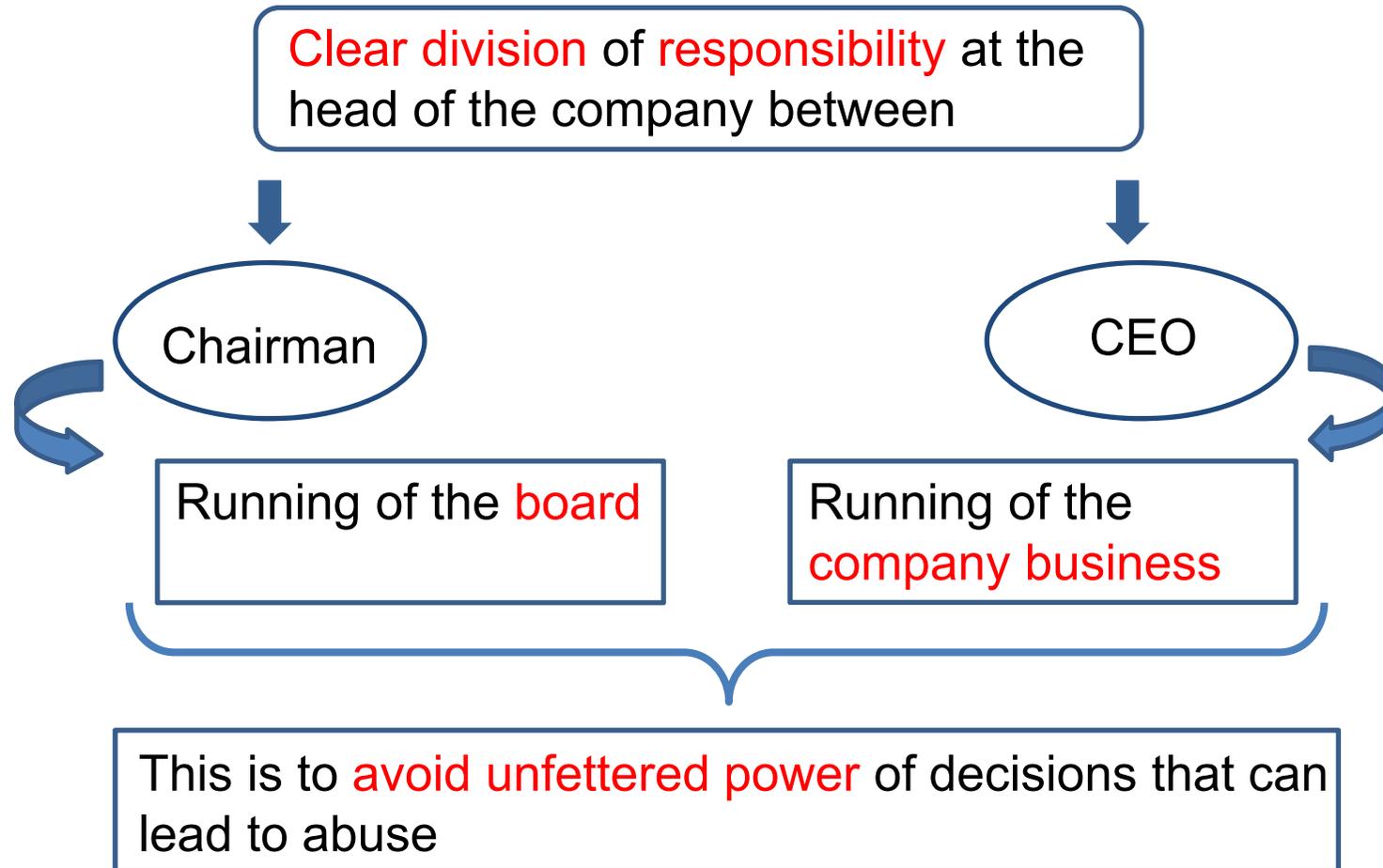
UK Corporate Governance Code's requirements:

- (a) Leadership**
- (b) Effectiveness**
- (c) Remuneration**
- (d) Relations with shareholders**
- (e) Accountability**

1) The Board



2) Chairman & Chief Executive



3) Board Balance & Independence

- The board should include a **balance** of **executive director and non-executive director** (especially independent non executive director)
- This balance should be such that **no one individual or group** of individual can **dominate** the **board's decision making**

4) Appointments of The Board

- **Procedure** for the **appointment of new directors** to the board should be **formal, rigorous & transparent**
- This calls for the **establishment of nomination committee** to promote meritocracy in the recruitment of director

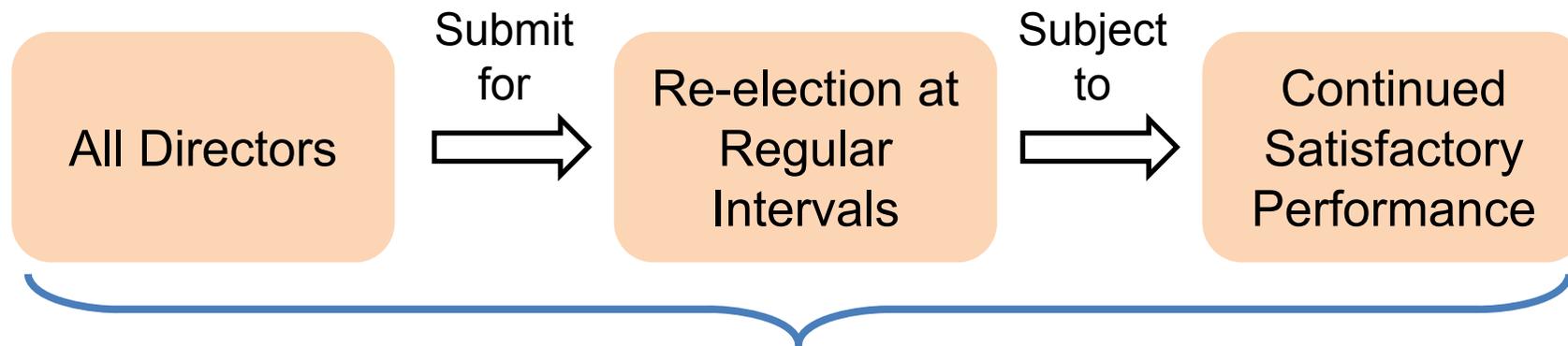
5) Information & Professional Development

- **Information** should be **supplied to** the **board** in a **timely manner**
- **Information** supplied should be of **appropriate quality** to allow board to discharge their responsibility
- **All directors** should **receive induction** on joining the board & should **regularly update** and refresh their **skills and knowledge** to **narrow the gap** between them created by diversity in experience & knowledge.

6) Performance Evaluation

- **Annual evaluation** of its **own performance** should be **undertaken in a** formal and rigorous manner.
- **Evaluation** of its **committee and individual directors** should be undertaken in the **same manner**

7) Re-election



This would not only ensure the independence of the non-executive directors concerned but also allows minority shareholders a chance to vote out a particular director.

A planned and progressive refreshing of the board would ensure a smooth taking over of responsibilities by someone being 'groomed' for the succession.

People

- Determine the appropriate level of remuneration for executive directors
- To **appoint, remove senior management & oversee succession planning**

Performance

Scrutinise the performance of management in meeting agreed goals & objectives & **monitor the reporting of performance.**

Role of non-executive directors in corporate governance

Strategy

Constructively challenge & contribute to the development of strategy

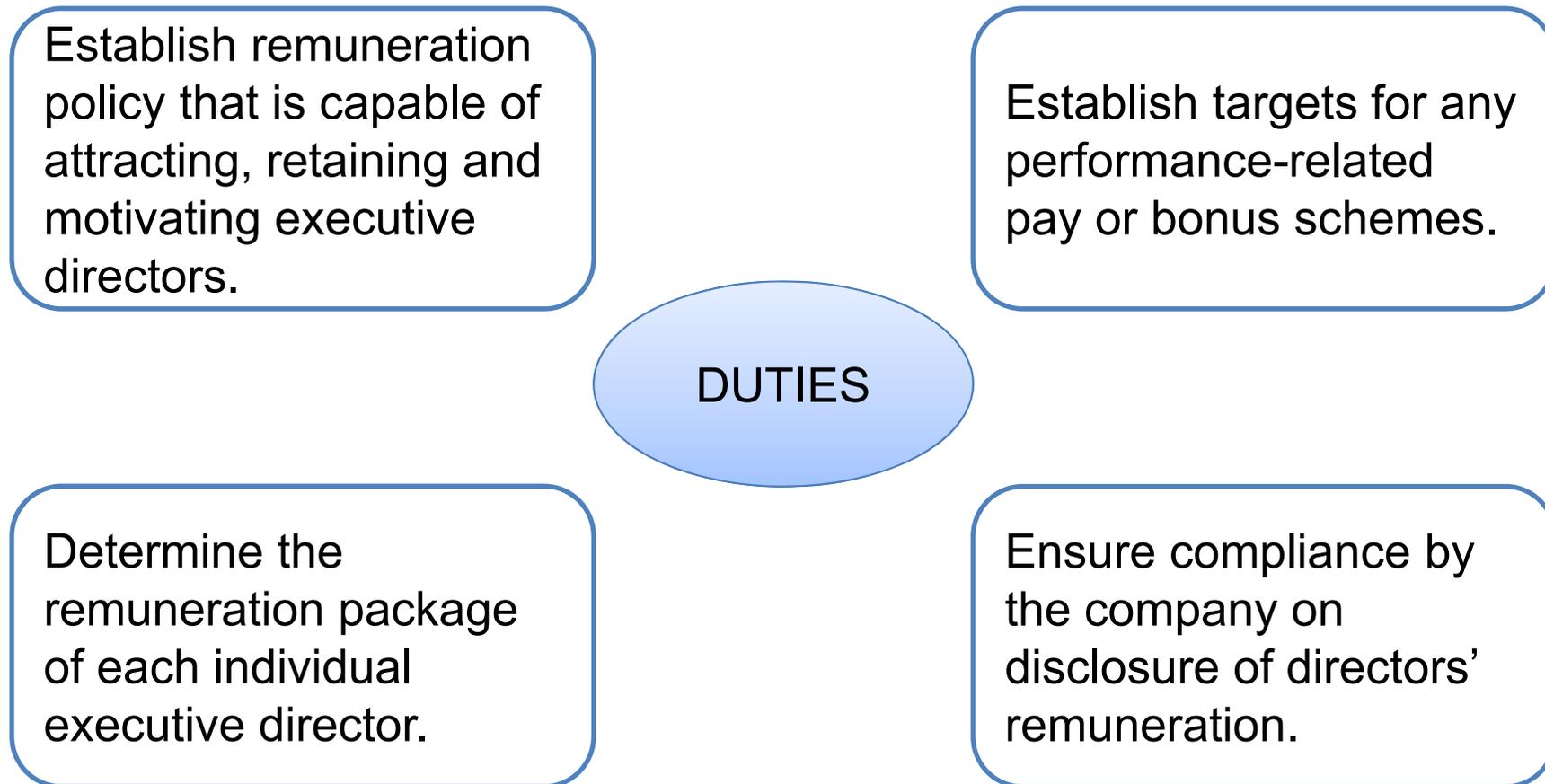
Risk

Satisfy themselves that:

- Financial information is accurate
- **Financial controls & system of risk management are robust.**

Remuneration committee

The UK Corporate Governance Code requires **all** members of the committee to be independent non-executive directors.





Nomination committee

The UK Corporate Governance Code requires a **majority** of members of the committee to be independent non-executive directors.

Duties

- Recruit new directors after considering the composition of the board in terms of the ratio and number of executive and non-executive directors as well as the diversity in knowledge and experience.
- Establish and review succession plans for the directors.
- Remove incompetent or unsuitable directors.
- Provide new board members with a comprehensive induction to board processes and policies and to their new role.
- Monitor and appraise each individual director's performance, behaviour, knowledge, effectiveness and values.
- Identify development needs and training opportunities for existing and potential directors.



Risk committee

Duties

- Champion and promoter of enterprise risk management across the group.
- **Oversee the implementation of the risk management policy.**
- Provide quarterly reporting and update on key risk management issues to the board.
- **Review enterprise risk profile for effectiveness of management of risks.**
- Evaluate any new risks identified by operating management.
- **Ensure that all action plans are acted upon and addressed.**
- Establish monetary threshold and nature of proposed investment that require risk committee's evaluation and endorsement before submitting to the board.



Audit committee

- Oversee financial reporting and internal controls
- Review the scope and outcome of the audit as well as the objectivity of the auditors.
- Provide a useful bridge between both internal and external auditors and the board
- Oversee the arrangements for whistle-blowers
- Assess the systems in place to identify and manage financial and non-financial risks in the company

Issues involving directors' remuneration

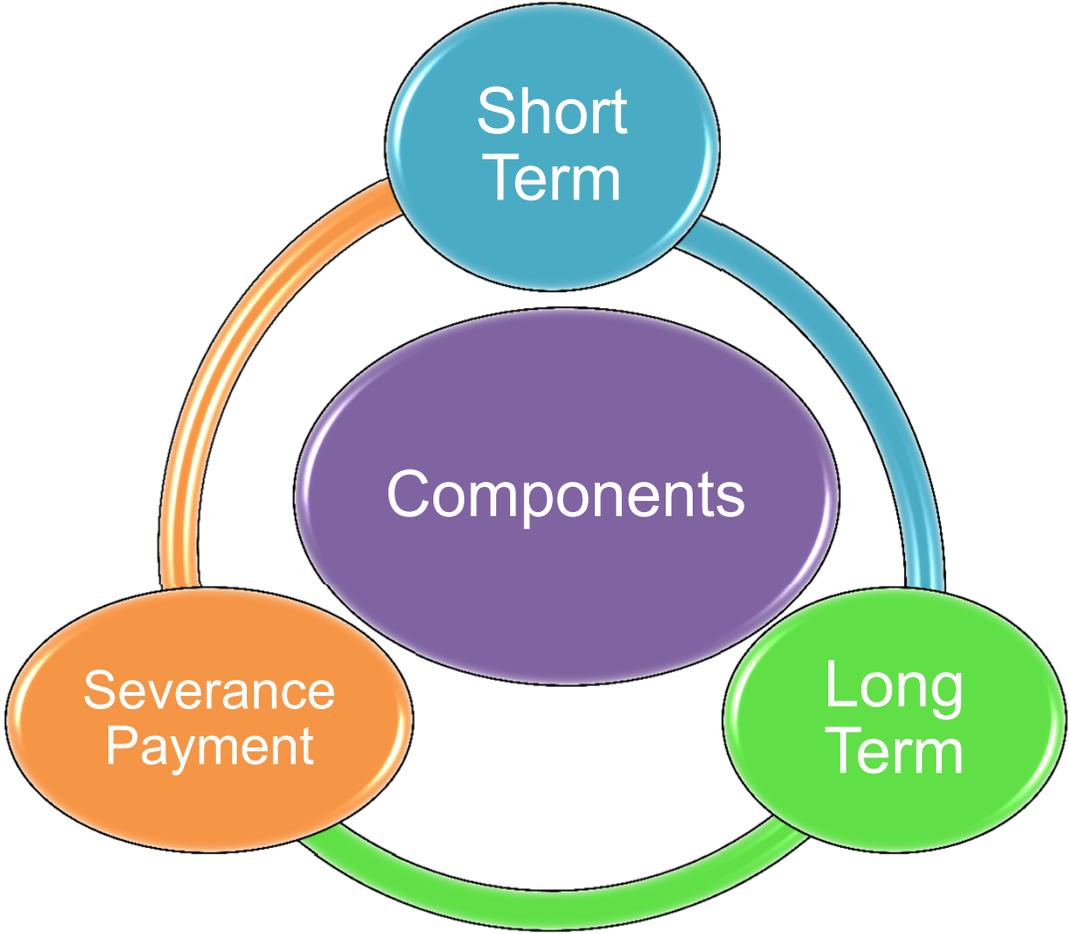


Remuneration
not linked to
company's
performance

Failure to
attract, retain
or motivate
the directors.

Chief executive officer
and executive
chairman are involved
in determining their
own remuneration
package.

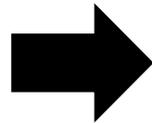
Components of director's remuneration



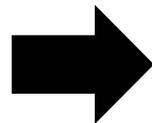
Components



SHORT-TERM



- Not related to the performance of the company nor the performance of the individual director.
- Set with regard to the size of the company, industry sector, experience of the individual director and level of base salary in similar company.



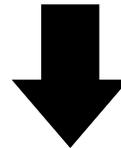
- Tied perhaps to the annual financial performance of the company.

Components

SHORT-TERM



Perquisites



- Various perks such as membership of the company's health insurance scheme, private use of the company's aircraft or boats, and so on are offered to directors to **reflect directors' status** as senior management of the company.

Components

Long-term

Share
Option

Grant directors the right to purchase shares at a specified exercise price over a specified time period.

company shares
(also known as
'restricted stock
grant')

Unlike option, directors paid **nothing** for these grant and therefore has value unless the share price goes down to zero. They are usually **awarded with limits on its transferability** for a set time but sometimes for the director's tenure with the company.



Components

Severance Payment

- The service contract of a director sets out the terms and conditions of his or her appointment, including the duration of the appointment and the required minimum period of notice of termination.
- In lieu of notice, the company is committed to giving the individual a minimum severance payment if he or she is **forced to leave** the company.

Performance related incentives

Pros



Rewards executive directors with one or more cash bonus payments, if actual performance during a review period **reaches or exceeds certain predetermined targets**.
→ help promote accountability to the shareholders.

The establishment of performance targets is in line with the concept of transparency.

Performance related incentives



Cons

Should the performance targets be for an annual period, **short termism practices** may be encouraged.

Profit measures which are often used as a basis for a reward system can be **manipulated** within the accounting rules by adopting more aggressive accounting policies and judgements.

Issues involving share options

- Executive directors treat share options as compensation, they **nearly always sell the share** for the cash thereby defeating the purpose of making directors the shareholders of the company.
- Stock option is only affected by price appreciation which inevitably encourages directors to **forgo increasing dividends** in favour of using the cash to try to increase the stock price.
- Directors are motivated to choose a **higher risk business strategy** that promises higher returns.

Two ways to maintain good relations with the shareholders:



1. Disclosure

Refers to mandatory and voluntary information produced by companies aim at **removing information asymmetry** caused by separation of ownership and control.



2. Communication

Refers to regular and constructive **two-way** communications between the company and its shareholders in the form of dialogues.

Types of Communication

Dialogue

Companies are encouraged to enter into dialogues with its institutional investors based on the **mutual understanding of objectives.**

Annual General Meeting

The board should make constructive use of the annual general meetings to **communicate with private investors** and **encourage their participation.**

Company's Website

Shareholders and investors will benefit from **timely information**, delivered perhaps through the company's website on a regular basis, about current developments in the company's affairs.

Annual Report

Financial position of the company and non-financial information such as the direction the company is taking, its strategic objectives, and so on can be found in this report.

Voluntary Disclosure

Characteristic



Disclosures that are **over and above** the mandated minimum. Examples include operating and financial review, management forecast, environmental or social report.

Benefit



Increased and improved disclosure is likely to **reduce agency costs** as better information flows from the company to the shareholder helps reduce information asymmetry.

Voluntary Disclosure

Problem



- **Absence of guidance** on the type and form of information that the shareholders and other stakeholders require.
- The **lack of standardisation** in reporting format made comparison between companies difficult.
- Information disclosed are **not subjected to audit** which affect their credibility and thus reliability.

Situations to justify intervention by institutional investors

Instances where institutional shareholders and/or agents may want to intervene include:

- the company's strategy;
- the company's operational performance;
- the company's acquisition/disposal strategy;
- independent directors failing to hold executive management properly to account;
- internal controls failing;
- inadequate succession planning;

Situations to justify intervention by institutional investors

- an unjustifiable failure to comply with the Combined Code;
- inappropriate remuneration levels/incentive packages/severance packages; and
- the company's approach to corporate social responsibility.

Types and Purposes
of Internal Control

Important Areas

The Board's Roles in
Internal Control

Elements of a Sound
System of Internal
Control

Types of Internal Control

Financial

Helps ensure the reliability of internal and external reporting, safeguard the assets including the prevention and detection of fraud.

Operational

Facilitates the economical and efficiency of operations thereby helping the company to achieve its goals and objectives (effectiveness).

Compliance

Assists compliance with laws and regulations and also with internal policies with respect to the conduct of business.

Risk Management

Allows the company to take risks knowingly by managing risks that are significant to the fulfilment of a company's business objectives.

Elements of a Sound System of Internal Control

The [Turnbull Report](#) describes a sound system of internal control as comprises of:



Control Activities

Communication
Process

Monitoring

Control
Environment

Control Activities



Internal controls put in place by the company in the areas of **financial, operational, compliance and risk management**

Communication Process



Procedures for **timely reporting of control findings** to management and establishment of **whistle blowing arrangement** to enable malpractices involving senior management to be reported.

Monitoring



In the **absence of internal audit function**, the **board should assume the responsibility of monitoring the continued effectiveness of the internal control system** so as to be capable of **responding quickly to changes in the risks**.

Control Environment



Establishment of a **positive corporate culture, management style and employee attitudes** to control procedures.

Board's role in Internal Control

- Establishment of sound system of internal controls to safeguard shareholders' interest and investment.
- Setting up of audit committee comprising wholly of independent non-executive directors to oversee internal controls and whistle-blowing arrangement.
- Review from time to time the benefits of having an internal audit function if the company does not already have one.
- Undertake review of the effectiveness of the group's system of internal controls at least once annually and report to shareholders that they have done so.
- Preparation of statement of internal controls that details the control mechanisms, weaknesses found and their associated consequences and measures taken to overcome them.

Role of Internal Audit



The Institute of Internal Auditors defined internal auditing as:

- An independent, objective assurance and consulting activity designed to add value and improve an organization's operations.
- Helping an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

To achieve the said objectives, the following tasks are undertaken by internal auditors:

- Carry out checks on the financial controls possibly in collaboration with the external auditors.
- Undertake special investigation following allegations made by whistle-blower
- Examine financial and operating information for timeliness and accuracy of reporting.
- Investigate into an operation or activity to determine whether it is economical, efficient and effective.

- Review compliance by an organisation with particular laws and regulations.
- Investigate an organisation's risk management procedures in terms of:
 - **comprehensiveness** of the risks identified
 - **reasonableness** of the assessment of risks
 - **appropriateness** of the measures taken to address the risks

Factors to Consider in Determining the Need for Internal Audit



1) Scale of operation

- The higher **volume of transactions** increases the likelihood of errors.

2) Diversity and complexity of the company's activities

- Diversity complicates the company's operation and thus increases the chances of errors.

3) Number of employees

- Increase in employees' number makes **close monitoring of them difficult** and higher chances of recruiting a potential fraudster.

4) Cost/benefits considerations

- Decision should also take account of the **qualitative nature** of the costs and benefits such as the morale of the staff and prevention of fraud respectively besides the quantitative factors.

Factors that Determine The Internal Auditors' Independence



1) The level from which the department derives its responsibilities (also known as **organisational status**)

↳ **Internal auditor should report to the highest authority** i.e. the board or its designated audit committee to command the respect and cooperation from the auditees.

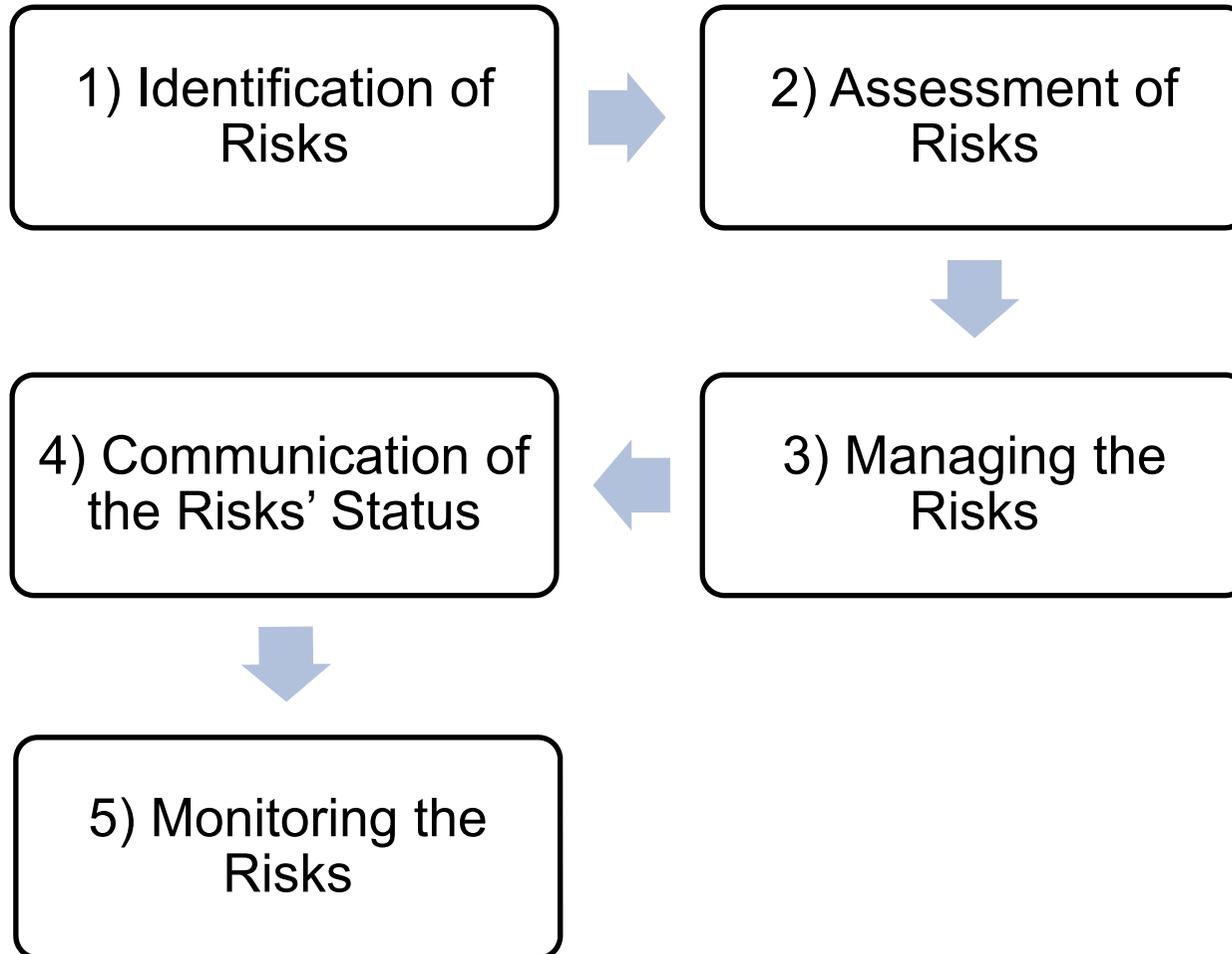
2) The **personality** of the senior management and head of department

↳ Internal auditors should possess an **independent mental attitude** that requires them not to be placed in situations where their objective professional judgements will be threatened.

Threats to Internal Auditors' Independence

- Undertake assignments where **relationship with the auditees exist**
- Assume **operational and management responsibilities** in the company
- Failure to observe a **reasonable period of cooling** for staff who has been transferred to or temporary engaged by the department.
- Involve in **designing, installing and operating systems** as well as **drafting procedures** for them

Risk Management Processes:



1) Identification of Risks



Risks that arise from strategic decision making/external environment and operations are being identified by the board and operating management respectively.

2) Assessment of Risks



Risks identified are then being measured in term of its likelihood of occurrence and impact on the organisation should it occur.

3) Managing the Risks



Depending on the significance of the respective risks, measures under the TARA framework are then implemented to mitigate or reduce the risks to an acceptable level.

4) Communication of the Risks' Status



The status of the risks are compiled and communicated by the Risk Manager to the Risk Management Committee on regular basis. They will in turn highlight the most significant risks faced by the company and the measures taken to rectify them to the board.

5) Monitoring the Risks



Since risks hardly remain static, they are monitored on a continuous basis to ensure that the company is able to respond to them promptly.

Categorisation of Risk are broadly based on their :



Severity



Nature



Sources

Severity

Strategic risks

- Risks that arise from an **organisation's positioning in the environment** and the **fundamental decisions made by the directors** on its objectives.
- Have the effect of **threatening the going concern** of the company.
- Responsibility for managing these risks lies with the **board**.

Operational risks

- Risks that are connected with the **internal resources, systems, processes and employees** of the organisation.
- Have the effect of causing **temporary hiccups** in the smooth running of an organisation's operations.
- Responsibility for managing these risk lies with the respective **line managers**.

Nature



Operational risks

Risks that threaten the **smooth running of an organisation** which can arise from breakdown of machineries, high staff turnover or interruption in the supply of raw materials.

Financial risks

Risks that have the effect of threatening a **company's cashflow** such as adverse movement in foreign exchange rate, hike in interest rate, default in payment from credit customers or overtrading.

Compliance risks

Risks that the company **failed to comply** with internal policies and procedures or external laws and regulations.

Sources

Risks are categorised based on **where they originate from**. Should the risk relate to reputation damaged, it will be termed reputation risk or research and development risk if it relates to failure to invest in research and development.

Types of Risk Assessment:

1) Qualitative

Word form or descriptive scales are used to describe the magnitude of potential consequences and the likelihood that those consequences will occur.

Example: Consequences – insignificant, moderate, catastrophic
Likelihood – almost certain, likely, rare

2) Semi-quantitative

Qualitative scales such as those described are given **values**. However, they **do not have to bear an accurate relationship** to the actual magnitude of consequences or likelihood

3) Quantitative

Numerical values rather than the descriptive scales are used for **both consequences and likelihood** using data from a variety of sources

TARA Framework:



Transfer the Risk



Avoid the Risk



Reduce the Risk



Accept the Risk

Avoid the risk

- Risk is avoided by **not proceeding** with the activity likely to generate the risk.
- Applicable for risks that have high chances of occurrence and the impacts are significant.
- Risk may also be inappropriately avoided because of an attitude of risk aversion

Accept the risk

- Risk is accepted if **both** the chances of its occurrence and the impact are **insignificant**.
- Risk can also be retained by default, when there is a failure to identify and/or appropriately transfer otherwise treat risk.

Reduce the risk

- Risk can be reduced via the **reduction in the likelihood** of occurrence or the **impact**.
- Measures taken include preventative maintenance, contract conditions, supervision etc. depending on the circumstances.

Transfer the risk (also know as sharing of risk)

- Risk is transferred if the impact is regarded as **too significant beyond the company's ability to tolerate**.
- Mechanisms include insurance arrangement, organisational structures such as partnership and joint ventures, outsourcing.
- The organisation to which the risk has been transferred, may not manage the risk effectively.

Related And Correlated Risk

- Related risks are those that often **present at the same time** in the same organisation because they have a common cause or that one type of risk can give rise to another.
- Correlated risks are those that **vary together** which can be negatively correlated (one goes up as the other declines) or positively correlated (both go up or down together).

Relativism

- Also known as pragmatic ethical assumptions
- This theory holds that because different societies have different ethical beliefs, there are no ethical standards that are absolutely true that apply or should be applied to the companies and people of all societies.
- An act is deemed ethical if it accords with the moral standards of people and companies in one particular society.

Absolutism

- Also known as **dogmatic ethical assumptions** and **universalism**.
- This theory maintains that there are **absolute moral truths**, **not relating to culture**, which **all entities must obey at all times** without exception.
- An **act** that is **deemed wrong in one country** is also wrong in **other countries**.

Kohlberg's stages of human moral development

- Divided into **3 levels** and **6 stages**.
- Conclusion can be reached through interview that consists of a series of dilemmas to judge the respondents reaction to them and the reasoning behind the answer.
- Helps us **understand how our moral capacities develop** and how we can become increasingly sophisticated and critical in our use and understanding of the moral standards we hold.
- Allows us to **manage the relationship with another parties better based on the level of moral development** they belong.

LEVEL 1:

Pre-conventional Morality

- Stage 1 people generally will not commit immoral or illegal activities due to their fear of punishment

whereas

- Stage 2 people will not mind doing it if they perceive such an act as a fair deal or it would not be found out.
- At this level, rights and wrongs are always defined in self-centred terms.

LEVEL 2:

Conventional Morality

- Stage 3 people will only undertake activities that are acceptable to his or her social groups.
whereas
- Stage 4 people perceives that social contract exist and so would not undertake activities that are against the interest of other members of society.
- At this level, right and wrong are defined in terms of the conventional norms of their social groups or the laws of their nation or society.

LEVEL 3:



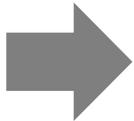
Post-conventional Morality

- Stage 5 people define moral **right and wrong in terms of moral principles they have chosen for themselves** as more reasonable and adequate. Calls for existing laws that do not promote the general welfare to be changed when necessary through majority decision, and inevitable compromise
whereas
- Stage 6 people believe that **justice carries with it an obligation to disobey unjust laws**
- At this level, rules are seen as not absolute dictates that must be obeyed without question. Individuals may disobey rules inconsistent with their own principles.

Teleological (consequentialist) approach to ethics

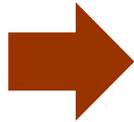
- Moral judgments are based on the outcome of a certain action.
- Consequentialist is a relativist.
- Two main theories namely
 - Egoism and
 - Utilitarianism

Egoism



- An **action** is **deemed morally right** if the **decision maker freely decides** in order to pursue either their short-term desires or long-term interests.
- Egoists are at **level 1 of Kohlberg's moral development** as their **action** is **motivated by self-interest**.
- Egoism based on desire is **criticised** for **rendering patently different approach to life as being equivalent** when long-term interest should be the deciding factor.
- This theory works fine only if mechanism exists in society to ensure that no individual egoist pursues his or her own interest at other egoist's expense.

Utilitarianism



- An action is **morally right** if it results in the **greatest amount of good** for the **greatest number** of people affected by the action.
- Utilitarianists are at **Stage 4** of Kohlberg's moral **development** as they **focus on the collective welfare produced by a certain decision**.
- This theory is **criticised** for the **subjectivity** involved in assessing and quantifying consequences such as pleasure or pain associated with an action.
- The interest of minorities is overlooked as the focus is on satisfying the greatest number.

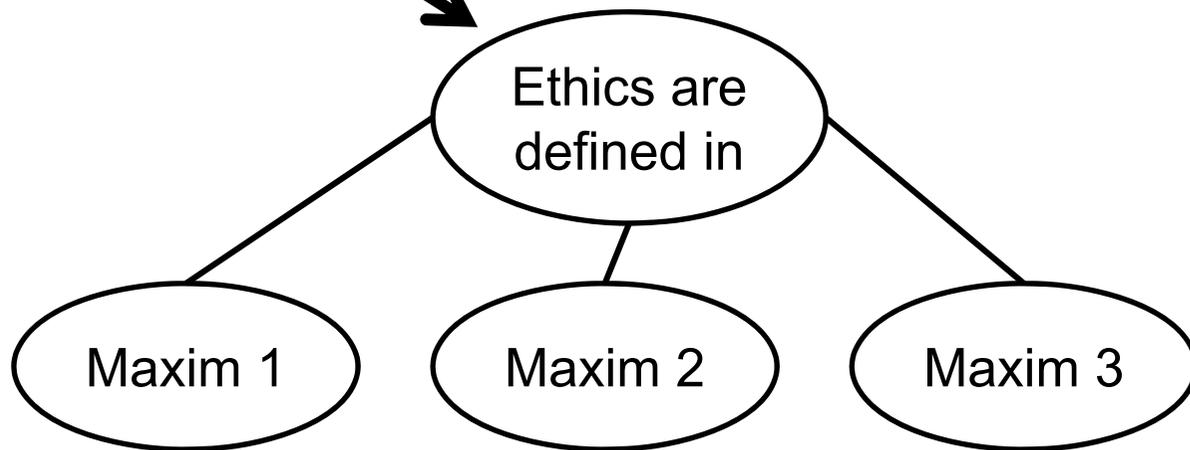
Deontological (non-consequentialist) approach to ethics

- Moral judgments are based on the underlying principles of the decision-maker's motivation.
- Non-consequentialist is an absolutist.
- Two main theories namely
 - Ethics of Duties and
 - Ethics of Rights & Justice

Also known as **Kantian Theory** or
Categorical Imperative Framework

Called for all human to behave ethically in accordance to eternal, abstracts and unchangeable principles all the time.

Ethics of Duties



Categorical Imperative Framework



Maxim 1

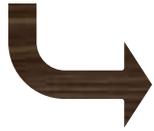
Act only according to that maxim by which you can at the same time view that it should become a **universal law**.

An action can only be right if everyone could follow the same underlying principle.

Maxim 2

Act so that you treat **humanity**, whether in your own person or that of another, **always as an end and never as a mean only**.

An action is right if human dignity is not being ignored.



Maxim 3

Act only so that the will through its maxim could regard itself at the same time as **universally lawgiving**.

An action is right if it is acceptable for every human being or is endorsed by them.

Ethics of Rights and Justice

- The notion of **rights** calls for humans to observe the rights **accorded to another person** and at the same time ensures **fair treatment** of individuals in a given situation with the result that **everybody gets what they deserved**.
- The rights approach has been very **powerful throughout history** and has substantially shaped the constitutions of many modern states and had **even led to United Nations declaration of human rights in 1948**.

American Accounting Association

- A **seven-step ethical decision-making model** that professional accountant can adopt for the **resolution of ethical dilemmas**.
- Encourages the decision maker to fully analyse the problem and to consider the alternatives and consequences from an ethical perspective.
- Provides insight from **both non-consequential considerations** (step 3 and 5) **and consequential considerations** (step 6) which is not achievable from a single theory.

Step 1: What are the facts of the case?

Provide a **summary of the dilemma experienced** by the decision maker in a given scenario.

Step 2: What are the ethical issue in the case?

Highlight the ways in which the relevant **stakeholders could be affected by the decisions made.**

Step 3: What are the norms, principles and values related to the case?

For decision makers who are **professional accountants**, **fundamental principles** such as **objectivity and integrity** will be relevant.

For decision makers that are **corporations**, **corporate governance concepts** such as **transparency and accountability** will be relevant.

Step 4: What are the alternative courses of action?

The possible courses of action will **depend on the scenario given**. Try to keep them to about four as for each course of action, there should be corresponding discussion on its **compliance with the norms, principles and values (step 5)** and **consequences (step 6)**.

Step 5: What is the best course of action that is consistent with the norms, principles and values identified in Step 3?

Benchmark each course of action against the identified norms, principles and values and make a conclusion.

Step 6: What are the consequences of each possible course of action?

Consequences can be either positive or negative and should be assessed from the perspective of own self, company or other stakeholders.

Step 7: What is the decision?

Decision can be a combination of options chosen from step 4 above instead of just one.

Conceptually slightly different from the AAA model but is nevertheless a **powerful tool for determining the most ethical outcome** in a given situation.

Tucker 5-question Model

Not all Tucker's criteria are relevant to every ethical decision

More useful for examining **corporate** rather than professional or individual situation

Profitable

Consideration is from the **perspective of the shareholders** to ensure that a proposed decision will **maximise the returns to them.**

Legal

An ethical decision is one that is **in line with the existing laws and regulations.**

Fair

Relates to the concept of justice such that **no one stakeholder** will be **inconvenienced or harm** by the decision made.

Right

A right decision is one that is **in line with the ethical theories.**

Sustainable or environmentally sound

Requires **the outcome of a decision to meet the needs of the present without compromising the ability of the future generation to meet their own needs.**

Gray, Owen & Adams' seven positions on social responsibility

Pristine
Capitalist

Expedient

Social
Contractarian

Social
Ecologist

Socialist

Radical
Feminist

Deep Ecologist

Pristine
Capitalist

→ Social responsibility is dominated by the need to make money for shareholders, to grow, make profits and seek economic efficiency.

Expedient

→ Certain (usually minimal) wider social responsibilities are accepted to ensure the long-term economic welfare and stability of a company.

Social Contractarian

Believes that companies and other organisations exist at society's will and therefore are obliged (to some degree) to society's wishes.

Social Ecologist

Calls for the change to the existing economic system which is responsible for the resource use, pollution, waste creation and the down grading of the quality of human life.

Socialist

Believes that the present domination of social, economic and political life by capital is unfavourable and promotes the re-adjustment in the ownership and structure of society.

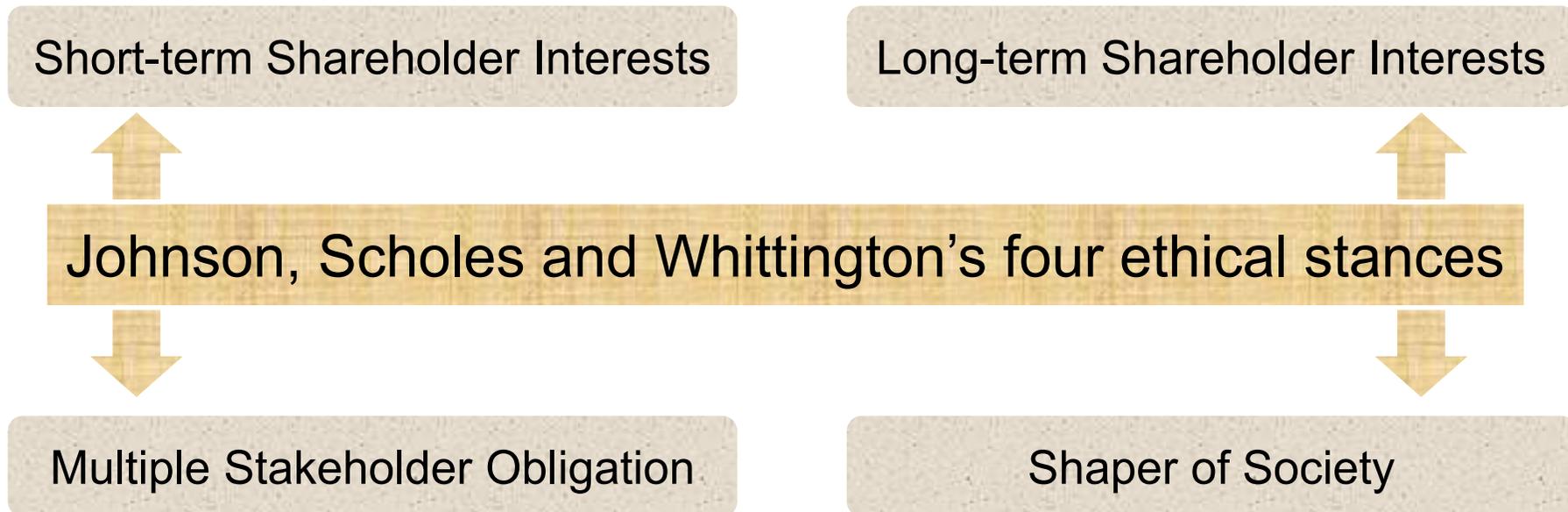
Radical Feminist

Criticises the existing social, economic, political and business systems for being too 'masculine' that emphasises on aggression, traditional success which denies a proper voice for compassion, love, cooperation and so on.

Deep Ecologist

→ Holds that human beings do not have any greater rights to existence than any other forms of life and criticises the common practice of contemplating trade-offs between the habitat of threatened species and economic imperatives.





Short-term Shareholder Interests

-  Takes the view that the only responsibility of business is the short-term interest of shareholders and any form of social responsibility must be prescribed through legislation and regulation.
-  This stance is similar to that of pristine capitalist.

Long-term Shareholder Interests

-  Recognises the importance of well-managed relationship with other stakeholders for the long-term financial benefits of the shareholders.
-  This stance is similar to that of the expedient.

Multiple Stakeholder Obligation



Believes that stakeholder interests and expectations should be more explicitly incorporated in the organisation's purposes and strategies beyond the minimum obligations of regulation and corporate governance.



This stance is similar to that of a social contractarian.

Shaper of Society



As the name suggest, the purpose of this group is to shape the society and financial considerations are regarded as of secondary importance or a constraint.



This stance is similar to that of social ecologists, socialist, radical feminist and deep ecologist.

Code of ethics for business conduct

↳ An authoritative statement of values and principles designed to **set a minimum standard of acceptable behaviour** and **guide organisational members in resolving ethical conflicts**

Advantages

- ✓ Provide a common value system for all divisions to adopt.
- ✓ Serves as a moral minimum that helps provide guidance in dealing with anomalies in local customs.
- ✓ Helps boost investors' confidence in the company.

Contents

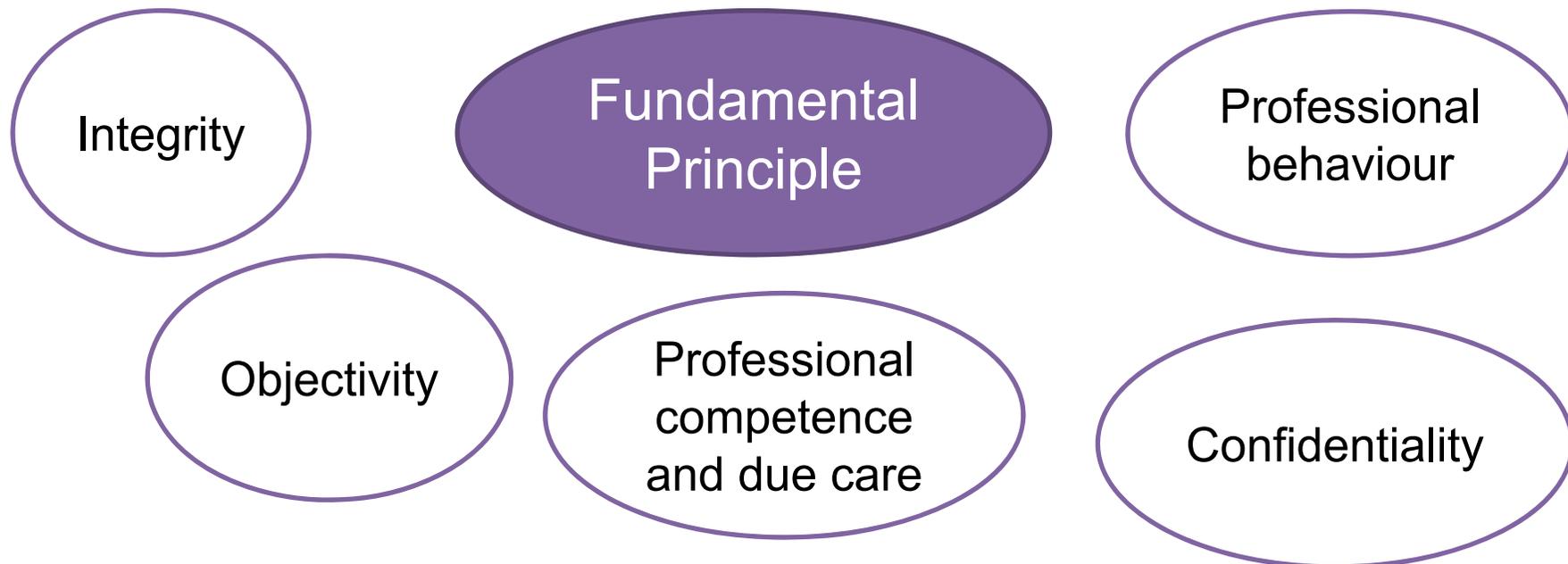


- Values of the business
- Senior management's commitment to doing business ethically
- Responsibilities of the respective parties in making the company ethical
- Key stakeholders of the company and the company's commitments towards them
- Whistle-blowing arrangement within the company
- Means to obtain advice, awareness raising examples (FAQ) and training programmes for all staff

Code of ethics for accounting profession



↳ The IFAC Code adopts a **conceptual framework approach** to complying with the fundamental principles of ethics that requires the professional accountants to **identify, evaluate and respond** to threats to compliance with those principles.



Fundamental Principle

Integrity

- ❑ Requires professional accountant to be straightforward (fair dealing) and honest (truthfulness) in all professional and business relationship.
- ❑ Should **not** be associated with reports, returns, communication or other information where they believe that the information:
 - (i) contains a materially false or misleading statement;
 - (ii) contains statement of information furnished recklessly; or
 - (iii) omits or obscures information required to be included.

Objectivity

Professional accountant should **not** allow **prejudice or bias, conflict of interest or undue influence** of others to override professional or business judgments.

Professional competence and due care

Professional accountants are obliged:

- ✓ to **maintain professional knowledge and skill** at the level that a client or employer will receive the advantage of competent professional service based on current developments in practice, legislation and techniques; and
- ✓ to **act diligently** in accordance with applicable technical and professional standards in all professional and business relationship.

Confidentiality

- Professional accountants should respect the confidentiality of information acquired as a result of professional and business relationships and **should not disclose** any such information to third parties **without proper and specific authority unless** there is a **legal or professional right or duty to disclose**.
- The need to comply with the principle of confidentiality **continues even after the end of relationships** between a professional accountant and a client or employer.

Disclosure is required by law:

- **Production** of documents or other provision of evidence in the course of **legal proceedings**; or
- **Disclosure to the appropriate public authorities** of infringements of the law that comes to light.

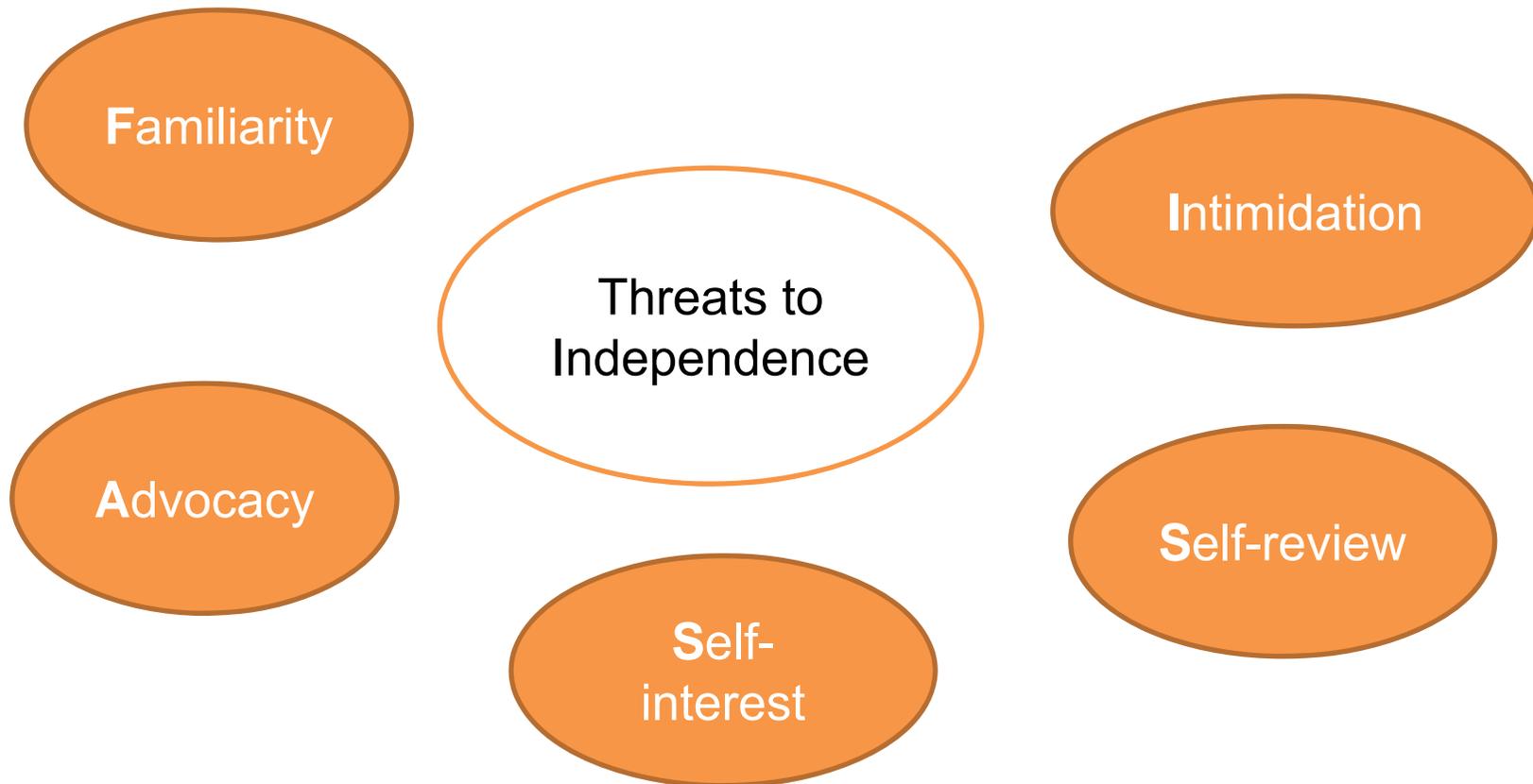
Disclosure is required by professional duty or right::

- to comply with the **quality review** of a member body or professional body;
- to **respond to an inquiry or investigation** by a member body or regulatory body;
- to **protect the professional interests** of a professional accountant in legal proceedings; or
- to **comply** with technical standards and ethics requirements.



Professional behaviour

A professional accountant should **comply with relevant laws and regulations** and should **avoid any action that discredits the profession.**



Threats to independence

Threat	Definition	Examples
Familiarity	Occurs when, by virtue of a close relationship with an assurance client, its directors, officers or employees, a firm or a member of the assurance team become too sympathetic to the client's interests	<ul style="list-style-type: none"> • a member of the assurance team having an immediate family member or close family member who is a director or officer of the assurance client • a member of the assurance team having an immediate member or close family member who is an employee of the assurance client, is in a position to exert direct and significant influence over the subject matter of the assurance engagement • a former partner of the firm being a director, officer of the assurance client or an employee in a position to exert direct and significant influence over the subject matter of the assurance engagement

Threat	Definition	Examples
Familiarity		<ul style="list-style-type: none"> • long association of a senior member of the assurance team with the assurance client • acceptance of gifts or hospitality, unless the value is clearly insignificant, from the assurance client, its directors, officers or employees
Advocacy	Occurs when a firm, or a member of the assurance team, promotes, or may be perceived to promote , an assurance client's position or opinion to the point that subsequent objectivity may be compromised	<ul style="list-style-type: none"> • dealing in, or being a promoter of shares or other securities in an assurance client • acting as an advocate on behalf of an assurance client in litigation or in resolving disputes with third parties

Threat	Definition	Examples
Self-interest	Occurs when the firm or member of the assurance team could benefit from a financial interest in, or other self-interest conflict with , an assurance client.	<ul style="list-style-type: none"> • a direct financial interest, or material indirect financial interest, in an assurance client • a loan or guarantee to or from an assurance client, or any of its directors or officers • undue dependence on total fees from an assurance client • concern about the possibility of losing the engagement • having a close business relationship with an assurance client

Threat	Definition	Examples
Self-interest		<ul style="list-style-type: none"> • potential employment with an assurance client • contingent fees relating to assurance engagements
Self-review	<p>Occurs when:</p> <ul style="list-style-type: none"> • any product or judgment of a previous engagement needs to be re-evaluated in reaching conclusions on the assurance engagement; or 	<ul style="list-style-type: none"> • a member of the assurance team being, or having recently been, a director or officer of the assurance client • a member of the assurance team being, or having recently been, an employee of the assurance client in a position to exert direct and significant influence over the subject matter of the assurance engagement

Threat	Definition	Examples
Self-review	<ul style="list-style-type: none"> a member of the assurance team was previously a director or officer of the assurance client or was an employee in position to exert direct and significant influence over the subject matter of the assurance engagement 	<ul style="list-style-type: none"> performance of services for an assurance client that directly affect the subject matter of the assurance engagement the preparation of original data used to generate a financial report or preparation of other records that are the subject matter of the assurance engagement

Threat	Definition	Examples
Intimidation	Occurs when a member of the assurance team may be deterred from acting objectively and exercising professional skepticism by threats, actual or perceived , from the directors, officers or employees of an assurance client	<ul style="list-style-type: none"> • threat of replacement over a disagreement with the application of an accounting principle • pressure to reduce inappropriately the extent of work performed in order to reduce fees

Impact of economic activity on the environment and society

Environmental footprint

The **impact** that a business's activities have **upon the environment** including its resource environment and pollution emission. Examples include the depletion of natural resources that are not renewable, rising temperature etc.

Social footprint

The **social impact** that a business activities have through the provision of products and services, the employment of workers, or some other corporate activity. Examples include the closure of plant on individuals and communities, erosion of local culture and environment etc.

The typical contents of social and environmental report



- A description of the company's activities at the site considered
- An assessment of all the significant environmental issues of relevance to the activities concerned
- A presentation of the company's environmental policy, programme and management system implemented at the site concerned
- A summary on the figures on pollutant emissions, waste generation, consumption of raw material, energy, water, noise

The typical contents of social and environmental report

- Other significant environmental aspects as appropriate, as well as other factors regarding environmental performance
- Significant changes since the previous statement
- The name of the accredited environmental verifier
- The deadline set for submission of the next statement.

An environmental audit typically contains three elements:



Agreed metrics (what should be measured and how)

Typical measures include measures of emissions and consumption which are essentially the organisation's environmental footprint.



Performance measured against those metrics

Target may be set for each of the metrics which then allows a variance to be calculated against the target.



Reporting on the levels of compliance or variance.

The data gathered from the audit enables metrics to be reported against target or trend (or both). It is generally agreed that this level of detail in the report helps readers better understand the environmental performance of organisations.

Public sector governance

Differences	Private Sector	Public Sector
Ownership	Private	Country / State
Control	Private Owners / Directors, and Managers working on their behalf	National Government or local authority
Capital	Raised by private owners	From Treasury
Use of Profit	Distributed to owners	Handed to Government or local authority
Aim	Profit – oriented	Service provision



Good governance in the public sector

The Chartered Institute of Public Finance and Accountancy (CIPFA) and the International Federation of Accountants (IFAC) had jointly developed the International Public Sector Governance Framework (International Framework) which outlined the following key principles of good governance in public sector.

- Strong commitment to integrity, ethical values, and the rule of law

The public sector is normally responsible for using a significant proportion of national resources raised through taxation to provide services to citizens. Public sector entities are therefore accountable not only for how much they spend but also for the ways they use the resources with which they have been entrusted.



- Openness and comprehensive stakeholder engagement

Public sector entities are run for the public good, so there is a need for openness about their activities and clear, trusted channels of communication and consultation to engage effectively with individual citizens and service users, as well as institutional stakeholders.

- Defining outcomes in terms of sustainable economic, social, and environmental benefits

The long-term nature and impact of many of the public sector's responsibilities mean that it should define its planned outcomes, which must be sustainable.



- Determining the interventions necessary to optimize the achievement of intended outcomes

Determining the right mix of interventions is a critically important strategic choice that governing bodies of public sector entities have to make in order to ensure they achieve their intended outcomes.

- Developing the capacity of the entity, including the capability of its leadership and the individuals within it

Public sector entities should develop its capacity as well as the skills and experience of its leadership and individual staff members to ensure that it operates efficiently and effectively and achieve its intended outcomes within the specified periods.



- Managing risks and performance through robust internal control and strong public financial management

Risk management and internal control are significant and integral parts of a performance management system and crucial to the achievement of outcomes while a strong system of financial management is essential for enforcing financial discipline, strategic allocation of resources, efficient service delivery, and accountability.

- Implementing good practices in transparency and reporting to deliver effective accountability

Effective accountability is concerned not only with reporting on actions completed but ensuring stakeholders are able to understand and respond as the entity plans and carries out its activities in an open manner.