

# IPBA Journal

September 2021

No **103**

NEWS & LEGAL UPDATE

Corporate  
Governance  
and Ethics:  
The New  
Challenges



INTER-PACIFIC  
BAR ASSOCIATION



**IPBA**  
TOKYO 2022  
20-23 APRIL

IPBA Annual Meeting and Conference in Tokyo 2022  
**Wisdom for the next 30 years**



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**IPBA 2022 Tokyo**

The Inter-Pacific Bar Association (IPBA) established in April 1991 at an organizing conference held in Tokyo is an international association of business and commercial lawyers who live in, or have a strong interest, in the Asia-Pacific region. IPBA 2022 provides the collaboration of ASEAN countries, seeing a more integrated approach of doing business and creating opportunities across and even beyond its reach.

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# IPBA Journal

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# The President's Message

Jack Li  
President



## Virtual World: Connecting You and Me

Dear Colleagues, Members and Friends, Brothers and Sisters,

### IPBA Virtual Conference 2021

The IPBA Virtual Conference 2021 was really impressive. Close to 400 delegates attended the conference and nearly 200 panellists spoke. This is the first fully virtual conference held right after the Annual Meeting and Conference in Shanghai under the devastating impact brought about by the COVID-19 Pandemic. I do appreciate the joint efforts and collaborations from all members and officers working for the IPBA during such a difficult time.

We were honoured to have Professor Richard Susskind OBE present his keynote speech for us at the conference. In Richard's latest book, *Online Courts and the Future of Justice, Tomorrow's Lawyers, the Future of the Professions*, we may realise his prediction for tomorrow's legal industry and the legal profession to adapt their way of work in cyber time. He notes the decline of today's professions and discusses the people and systems that will replace them. In an Internet society, the argument is that we will neither need nor want doctors, teachers, accountants, architects, the clergy, consultants, lawyers and many others, to work as they did in the 20th century. The Future of the Professions explains how 'increasingly capable systems'—from telepresence to artificial intelligence—will bring fundamental change in the way that the 'practical expertise' of specialists is made available in society.

### 1. Online Technology Has Changed Legal Proceedings Profoundly

COVID-19 has accelerated the number of parties choosing virtual hearings, but this is not the first time that proceedings have been convened with

the use of technology. From the early days of technology, some courts or tribunals have been willing to convene hearings of urgent applications by telephone and have allowed witnesses to be heard remotely using video conferencing facilities, and some even provided for their own rules or protocols as to remote witnesses.

For this point, many complex commercial disputes are known to have many difficult commercial and legal documents. Digital, searchable documents are easier to navigate, organise and position via screen sharing, ultimately reducing time often wasted when trying to locate a page of an exhibit. It is hugely time consuming, especially as many cases may involve more than ten parties, including witnesses, experts, counsel, and for tribunals, whose hearings conducted under the traditional on-site method. I imagine that there will be a positive impact in respect of the complex commercial dispute landscape in this regard.

### 2. Will AI-Based Systems Replace Lawyers?

The advanced technology of artificial intelligence ('AI') is already distributed across industries and helps to renovate this space broadly by driving solutions efficiently. The innovative nature of artificial intelligence features helps many enterprises and professionals to operate more efficiently than before. So, will AI-based systems replace lawyers?

In my view, AI won't replace lawyers, but lawyers who use AI will replace those who don't. As machine intelligence rapidly improves, the value of human predictions without AI enhancement will likely decrease. Artificial intelligence and

machine learning have already arrived in many law firms and legal departments. It will change the way we make decisions—employing machine-derived predictions as a complement to human judgment. The value of human judgment that is enhanced by machine analysis and predictions will thus increase. Therefore, for lawyers and law firms who embrace artificial intelligence and other advanced technologies, legal work will become

more efficient and effective. More importantly, clients will demand it. Increasing sophistication in client technology adoption will apply pressure on law firms and lawyers, who will be selected for their technology-enhanced services and ability to focus on complex higher-value work to solve their clients' legal and business problems.

**Jack Li**  
President

## Publications Committee Guidelines for Publication of Articles in the IPBA Journal

We are pleased to accept articles on interesting legal topics and new legal developments that are happening in your jurisdiction. From time to time, issues of the Journal will be themed. Please send: (1) your article to both **Priti Suri** at p.suri@psalegal.com and **James Jung** at jjung@collaw.edu.au; (2) a lead paragraph of approximately 50 or 60 words, giving a brief introduction to, or an overview of the article's main theme; (3) a photo with the following specifications (File Format: JPG or TIFF, Resolution: 300dpi and Dimensions: 4cm(w) x 5cm(h)); and (4) your biography of approximately 30 to 50 words.

The requirements for publication of an article in the *IPBA Journal* are as follows:

1. The article has not been previously published in any journal or publication;
2. The article is of good quality both in terms of technical input and topical interest for IPBA members;
3. The article is not written to publicise the expertise, specialization, or network offices of the writer or the firm at which the writer is based;
4. The article is concise (2500 to 3000 words) and, in any event, does not exceed 3000 words;
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## The Secretary-General's Message

**Yong-Jae Chang**  
Secretary-General



Dear IPBA Members,

I am writing to you after my first few months as Secretary-General of the IPBA to thank all of you for continuously supporting this special organisation in these challenging times. I would also like to express my gratitude to Michael Burian, my predecessor, for his great efforts and cooperation to improve various aspects of the IPBA during his term. Many of our members put more time into our organisation for preparing and attending various webinars and virtual conferences while having to make difficult decisions collectively in such an unprecedented environment with continued travel restrictions or prohibitions. In this regard, my special thanks to Rhonda and Yukiko for working extremely hard to maintain and coordinate our activities and events successfully even though these were rescheduled a number of times due to the global pandemic situation.

By working together and supporting each other, we were able to organise and implement several successful events, including the first online Annual General Meeting in 2020, our 30th Annual Meeting and Conference in Shanghai in April 2021 (held as a combined onsite/online event) followed by the IPBA Virtual Conference in June 2021, as well as numerous webinars and online meetings in between. It was our first virtual conference, with the theme 'Innovative Resilience in an Altered Legal Landscape' that featured a plenary session with a keynote by Professor Richard Susskind OBE, President of the Society for Computers and Law, Chair of the Advisory Board of the Oxford Internet Institute, and technology advisor to the Lord Chief Justice of England and Wales. Furthermore, there were opening remarks from our President Jack Li, 36 concurrent sessions and many online networking opportunities, all culminating in the IPBA Annual General Meeting. My sincere congratulations to our President Jack Li, together with the organising committee and everyone who helped making these special and successful events.

The IPBA Mid-Year Council Meeting and Regional Conference is now planned to be held virtually again later this year from 13 to 15 November 2021 and we will continue to provide an online platform that is easily accessible and that offers all participants the opportunity to participate and connect to one another for social networking sessions.

With more rollout of vaccines, we are now cautiously optimistic about being able to travel to Tokyo next year for the 31st Annual Meeting and Conference. The conference theme is 'Wisdom for the Next 30 Years' and it will be the fourth time the IPBA will hold its Annual Meeting and Conference in Japan. I greatly appreciate our President-Elect, Miyuki Ishiguro, and the host committee for preparing and organising this important event in quite uncertain times. I truly hope that we will all be able to meet in person in Tokyo from 19 to 23 April 2022.

While I am very proud of our strenuous endeavour to deal with onerous tasks and find alternative solutions so far to achieve our key objectives for the IPBA, it is likely that there will be more challenging issues affecting the IPBA during my term as Secretary-General. We all need the IPBA members' support more than ever and I will do my best to ensure that this extraordinary organisation will remain resilient and ready to resolve many outstanding (yet difficult) tasks in order for us to keep growing together in the right direction. We are still learning (hopefully positive) lessons from the enduring impacts caused by the current pandemic crisis and, in the meantime, I wish all of you good health and the strength we all need to eventually overcome the pandemic.

**Yong-Jae Chang**  
Secretary-General





## Message to the Reader

Dear Reader,

Welcome to the September issue of the IPBA Journal. The theme is "Corporate Governance & Ethics: The New Challenges." With the pandemic charting its own course across the world, boards face difficulties like never before and relying on past practices does not seem to work. The new environment throws up complex pressures and demands from each stakeholder which are tough to manage given the uncertain times we live in. Consequently, decision making is not easy. As the world learns to live with a "new normal," boards will have to monitor relationships with their core stakeholders more proactively.

In the present edition, six authors cover a wide array of related themes. In the first article, "The European Union Project on Sustainable Governance" Sara Marchetta examines the EU project on sustainable governance and the innovative position of regulators, both for business and on ethics. Then, James Bui adds a Vietnamese perspective and discusses "Ethics and Governance in the Digital Age and Challenges for Enterprises" and makes a case of how it is necessary to juggle and balance common interests of all stakeholders. In the third article "Humanisation into a Good Corporate Citizen" two co-authors, Dej-Udom Krairit and Kanitta Petchsoongsakul, explore Thai practices while resolving problems and creating sustainable living through laws, regulations and innovative business frameworks.

Thereafter, in "Corporate Governance in UAE: The New Challenges" Mohammed Alsuwaidi examines how the enhanced focus on corporate governance will promote the country's position as an attractive locale for investment. In the fifth article titled "Corporate Governance & Ethics: A New Challenge to Corporate Governance" Monchai Varatthan examines the board's role to create a top-down effective culture of corporate

governance and ethics. The final article is on "Challenges in Corporate Governance in India Post-Pandemic" where Srishti Singhania discusses the need to resolve corporate governance challenges to support recovery and booster growth.

This edition does not contain our now regular feature "Up Close and Personal" but we shall be back with that in December. In addition, there are details about new members between June 2021 and August 2021. Please continue to share professional milestones for the journal. A request for call for articles for the last edition of 2021 shall go out early October and we hope that we shall see contributions from new members and countries! The journal is a great way to get more engaged with the IPBA!

Thank you, as always, for your interest and consistent contributions. My Vice-Chair, James Jung, and I both remain grateful.

**Priti Suri**  
Chair – Publications Committee, IPBA

## IPBA Upcoming Events

Event	Location	Date
<b>IPBA Annual Meeting and Conferences</b>		
31st Annual Meeting and Conference	Tokyo, Japan	April 19-23, 2022
32nd Annual Meeting and Conference	Dubai, UAE	March 6-10, 2023
<b>IPBA Regional Conference</b>		
IPBA East Asia Regional Forum	Tianjin, China	September 25, 2021
<b>IPBA Mid-Year Council Meeting</b>		
2021 Mid-Year Council Meeting and Regional Conference	Online	November 13-15, 2021
<b>IPBA Webinars</b>		
Telemedicine and Digital Health Data in Asia: Regulatory Trends or Gaps, and Issues	Online	September 9, 2021
Trade Remedies Update	Online	September 14 and 16, 2021

More details can be found on our web site: <http://www.ipba.org>  
The above schedule is subject to change.

## Join the Inter-Pacific Bar Association

Since its humble beginnings in 1991 at a conference that drew more than 500 lawyers from around the world to Tokyo, the IPBA has blossomed to become the foremost commercial lawyer association with a focus on the Asia-Pacific Region. Benefits of joining IPBA include the opportunity to publish articles in this IPBA Journal; access to online and printed membership directories; and valuable networking opportunities at our Annual Meeting and Conference as well as 10 regional conferences throughout the year. Members can join up to three of the 24 committees focused on various of commercial law practice areas, from banking and finance, to insurance, to employment and immigration law, and more. We welcome lawyers from law firms as well as in-house counsel. IPBA's spirit of camaraderie ensures that our members from over 65 jurisdictions become friends as well as colleagues who stay in close touch with each other through IPBA events, committee activities, and social network platforms. To find out more or to join us, visit the IPBA website at [ipba@ipba.org](mailto:ipba@ipba.org).



# The European Union Project on Sustainable Governance

● ● This Article refers to sustainability as one of the ethical contents that has made its way into the business of corporations and in their governance, and has lately taken up much space in the discussions for a post-Pandemic reset of business values. In this respect, the EU project on sustainable governance expresses a quite innovative position of EU regulators, looking ahead for the meaning of businesses in our communities.



In the aftermath of the financial meltdown of 2008–2009, it became clear that one of the reasons for the crisis was inefficient governance by the boards of banks and other financial institutions and, more generally, by boards of investors and corporations. The general attitude of ‘tick the box’ and of delegating risk management and oversight of strategic decisions only to executives—heavily involved in the boards as well—together with a very strong focus on shareholders’ returns and on remuneration linked to financial performance only for managers, was heavily criticised, first in the Walker Review published in 2009 in the United Kingdom.<sup>1</sup>

A few years earlier, in the United States, the Sarbanes-Oxley (‘SOX’) Act in 2002 popularised the term ‘tone at the top’—meaning ethical leadership, including fairness, transparency, accountability and integrity in behaviour and approach to business, plus an active involvement of the directors, with an increasing role of the non-executive and independent directors. Following several audit and accounting scandals, the ‘tone at the top’ was to be reset for boards (and governance) of companies wishing to be successful in the long term, and resilient during major crises.

These principles were also later included in the definitions of the G20/OECD: ‘The purpose of

corporate governance is to help build an environment of trust, transparency and accountability necessary for fostering long-term investment, financial stability and business integrity, thereby supporting stronger growth and more inclusive societies.<sup>12</sup>

Already before the financial crisis of 2008 and 2009, under the leadership of the United Nations, a group of large global investors voluntarily subscribed to the Principles of Responsible Investment, therefore introducing in the investment world the now fashionable Environment, Social and Governance ('ESG') principles.<sup>3</sup> When the Member States of the United Nations adopted the 17 Sustainable Development Goals in 2015, as part of the 2030 Agenda for Sustainable Development, where global action, local action and people action were requested for reaching those goals, businesses—as part of the civil society of people—were also called to action.

At the same time, regulations for the main stock exchanges in the world (London, Hong Kong, New York and also the Italian CONSOB in Milan), at a different pace introduced the so-called non-financial reporting, in which companies should include—largely at the discretion of the reporting company—certain disclosures about matters concerning environmental and social issues, plus a separate Governance Report. Curiously enough though, in many corporations it was—or it still is—the communications department dealing with ESG matters, as they were or are mainly seen as part of the reputation and image of the company, beyond compliance matters. ESG—with special indications about governance and the role of the boards—was entering the world of listed companies, thanks to the push of investors and other stakeholders.

In the European Union ('EU'), the non-financial disclosure requirements were introduced by the so-called Non-Financial Reporting Directive in 2014,<sup>4</sup> which was implemented in the national legislation of the Member States in the subsequent years. The EU has further issued regulations in connection with shareholders' engagement (the Shareholders' Rights Directive)<sup>5</sup> and for facilitating sustainable investment (the Taxonomy Regulation).<sup>6</sup>

More recently, on one hand, the global COVID Pandemic accelerated this process and drew more attention to risks connected with the environment—such as climate change—and to social issues and,

on the other hand, the rise of Socialist China, with its state corporatism, as a new world superpower, both from an economic and a geopolitical point of view, have driven attention to the search for common 'fundamental values' in business, for governments, corporations and investors.

Corporations are also to clearly identify, along with their shareholders, the interests of their stakeholders (employees, local communities, regulators, suppliers and customers) partly on a voluntary basis and partly to comply with their reporting obligations. Key institutional investors have started to act on their commitments and proposals to support ESG matters, and the purpose of governance and compliance has been slowly including, beyond the traditional prevention of unlawful conduct, the promotion of responsible conduct, for a more positive and proactive role of businesses, both in terms of directors' duties and in terms of stewardship obligations for investors and asset managers. As the shift in focus is taking place, soft law standards—and voluntary undertakings—are not considered enough anymore for real action in terms of ESG in the business world.

The approach to ESG—environment and social issues, but also governance—has moved from a 'do no harm' to a 'do good while doing no harm' attitude<sup>7</sup> and investors (pension funds, general partners of private equity funds, sovereign funds) are quickly abandoning the 'exclusion' principles—in which they would just exclude from their portfolios companies with a low ESG rating—to adopt a more proactive, scouting attitude in which they look to include good ESG performing targets. Companies have quickly learned that a proactive attitude, beyond compliance with regulations, is very well received by all their stakeholders. The initial 'do no harm' principle was not enough when trying to solve ethical dilemmas such as matters in the supply chain and could in fact be used as an excuse for not acting.

Also, in COVID times, and especially at the end of 2020, it became clear that corporations which had better ESG scoring were also performing better financially and were in general more resilient than others during the Pandemic.<sup>8</sup>

In such context, the EU last year started a project to renew and reset the criteria for governance of corporations, with a view to creating a sustainable



governance framework for EU companies and for non-EU companies operating in the EU market.

The European Green Deal already indicated that sustainability should be further embedded in corporate governance<sup>9</sup> in order to frame corporate decisions on their environmental, social, human and economic impact.

The project was started after several studies highlighted that pressure to generate short-term results for shareholders, especially in listed companies, has impacted corporations' ability to focus on long-term development and the sustainability of their strategic decisions. Remuneration and incentives to executives—linked only to return to shareholders and share price performance—have also been to the detriment of other employees and of the assessment of risks and impact of corporate actions. Failure to integrate sustainability actions into business decisions could also lead to missing new opportunities and an inability to build resilience. A narrow interpretation of directors' duties and shortcomings in corporate legislation has led to corporations not sufficiently covering the interests of stakeholders different from shareholders and executives.<sup>10</sup>

Finally, at the end of 2020, the European Parliament issued a resolution calling on the European Commission's action in the field of company law and corporate governance, considering that voluntary action has not proven efficient in enhancing sustainability at a corporate level, as obviously corporations which have been frontrunners of sustainability face issues of a level playing field. In particular, the EU Parliament calls for new regulations to clarify the directors' obligations versus long-term growth and sustainability and towards all the stakeholders and wider societal interests, and to address the shortcomings of current regulation on non-financial reporting in order to reduce the impact of 'short-termism'. Materiality thresholds for reporting should be assessed with the contribution of all stakeholders and incentives should be set to support action. Several detailed contents will be discussed during this year in connection with listed companies, such as reports of bribery and anticorruption issues, disclosure of employees' salaries,

mandatory audit of non-financial statements, reporting based on different tax jurisdictions, enhancement of the due diligence on supply chains, policies on fair salaries and gender equality for all employees.<sup>11</sup>

It is to be further noted that the EU approach to international treaties also includes sustainability, both in terms of general principles (the political covenant on the Comprehensive Agreement on Investment reached in December last year between the EU and China refers to 'sustainable investment' and includes several labour principles) and in terms of due diligence on supply chain (several already signed Free Trade Agreements, including the one with Vietnam).

The approach to ESG has moved from a 'do no harm' to a 'do good while doing no harm' attitude.

With regard to due diligence on the supply chain, where new regulations are on the way, generally applicable rules should be enacted with specific guidance on sectors, risk-based, proportionate and context-specific: this could achieve both purposes of including sustainability considerations in the management of the supply chains and the harmonisation of standards to ensure legal certainty and a level playing field.

Remuneration of executives should take into consideration the interests of the wider community, the employees and sustainable goals for the company as a whole.

As for the duties of directors, we expect that the relevant definitions will be clarified to avoid narrow interpretations and include in the interests of the company as a whole also the interests of all the stakeholders for long-term success, resilience and sustainability of the company (the 'sustainable success' of the Italian Corporate Governance Code 2020). Relevant regulations will also have to clarify whether stakeholders might enjoy an enforcement right over such duty of care of the directors.

Conversations on unlisted companies, and in particular SMEs, consider instead as preferable a set of voluntary governance principles, as investors in such companies are already committed to a medium or long-term purpose due to their restricted ability to trade their shares. These principles should of course take into consideration the size, complexity and maturity of

each company and could be applied in a flexible and pragmatic manner.

There is already further legislation and policies in the EU for reference on specific issues, such as the EU Pillar of Social Rights Action Plan (4 March 2021) and in other countries, and more is still to come.

The key question revolves around the meaning of business for society and whether corporations should have a wider purpose which goes beyond the profit of the shareholders. Existing governance arrangements have, for various reasons, failed to address certain risks and adverse impacts on global and local communities of operations of their corporations and therefore the definition of the company's purpose has become extremely important to mix and match the corporation's commitment to all stakeholders, for profit growth together with social responsibility.<sup>12</sup> And governance is the way such a relationship—between a corporation and its communities and stakeholders—is forged.<sup>13</sup>

I have particularly appreciated the definition of 'corporate purpose' elaborated by the law firm Wachtell, Lipton, Rosen & Katz: 'The purpose of a corporation is to conduct lawful, ethical, profitable and sustainable business in order to create value over the long-term, which requires consideration of the stakeholders that are critical to its success ... with regular engagement of the shareholders, who are essential partners in support of the corporation's pursuit of this mission'.<sup>14</sup> In this view, businesses are expected to have responsible conduct and provide a substantial and positive social contribution to their communities.

A next step for further discussion could be the so-called 'social licence to operate', which goes beyond the traditional corporate social responsibility to seek the agreement and the approval of all the stakeholders to a certain project.<sup>15</sup> This could be done more easily with a very specific project, including a locally restricted community. It is far more complex to achieve such a goal for multinational companies operating in different markets, with different stakeholders, when legitimacy, credibility and trust might have different form and substance.

Ethics from Greek philosophers to Hegel, from Confucius to Socialist China, and through the Christian religion or Buddhism, have taken different forms and content, and some of them have been in the past not particularly keen on business.

When we look at globalisation, at issues of climate change, at the economy and human capital in developing countries or at the history of the United States, Europe, Japan and China, we can consider that a level playing field should be allowed for all, basic rules of reciprocity should be set up and regulations for comparison among the performance of different corporations for the benefit of the public and of the investors' decision are due. The issue

here is obviously common standards, harmonised taxonomies and similar regulations for corporations of similar sizes. These rules should be mostly common—or at least comparable—in the main regions of the world. This might be easier, although still very complex and controversial, for environmental issues; however, it is a lot more difficult for social matters, which are also linked to the different values of different cultures and governments. We should not underestimate the impact of potential regulations on the development of different areas of the world, some of which have not yet developed an ESG approach for businesses, or if they have, like China,<sup>16</sup> have done so based on different underlying principles and values, at least for certain matters. As discussed above, a global environmental approach might be easier to agree upon, considering that many countries have committed to the Paris Agreement, the EU and China have committed to carbon neutrality by 2050 and 2060 respectively, and the US and China are leading the G20 Sustainable Finance Working Group.<sup>17</sup>

Governance and the boards of corporations have found themselves caught between the interests of shareholders and of stakeholders, among different values, backgrounds and cultures, and the need to cope with global investments and supply chains. Stakeholders and the general public are scrutinising—through obligations of reporting or explanations on why some issues are not included in the public reports<sup>18</sup>—injustices in diversity, equity, inclusion,

Until several years ago, companies were not very active on corporate ethics per se, but they were still supposed to assess their risks in order to take strategic decisions.

political contributions and lobbying efforts, health and wellbeing of employees and of local communities. The directors of corporate boards are expected to have a clear strategy and direct oversight on ESG—beyond reporting, and for integrating ESG principles in the strategic decisions and in the corporate operations—and, for better assurance, to have relevant data and targets assessed by third parties' audits. And where there is a crisis, the company board and the executives should share the risks and the difficulties—including review of remuneration—with the company's employees and other stakeholders.

Until several years ago, companies were not very active on corporate ethics per se, but they were still supposed to assess their risks in order to take strategic decisions. Furthermore, in terms of reputation, unethical behaviour, that is, deviation from generally accepted standards, could in fact be more damaging than the violation of codified regulation. Companies were expected to have good governance and good behaviour and to be good corporate citizens. This is the reason why many of them have adopted in the past years codes of conduct and/or ethics, a set of moral principles to guide the actions of the company, of its corporate organs and of its executives, in accordance with its purpose, to prevent practices which could harm the company.

At this moment in the EU, traditional corporate social responsibility, based on fair competition, legal compliance and voluntary actions for the benefit of the society, but still not related to the company, has been overridden by a wider commitment of responsible conduct, which includes responsible actions where there is a legal gap, compliance with the spirit of the law, alignment to stakeholders' values, evaluation of corporate impact from a social perspective, as part of the corporate strategy of wealth creation in the long-term. Companies are expected to promote higher standards of behaviour and to have the courage to uphold values, confront wrongdoing and push constructive change in their communities.

I believe that these principles could be shared among different cultures and business environments through constant dialogue and exchange in communities around the world and we as advisors could play an important role to foster change, also through international organisations like the IPBA.

## Notes

<sup>1</sup> Sir David Walker— former chairman of Morgan Stanley – published on 26 November 2009 a final review of corporate governance in banks and other financial institutions, offering guidelines for more efficient governance and more effective boards.

<sup>2</sup> G20/OECD, *Principles of Corporate Governance*, 2015.

<sup>3</sup> Launched in April 2006, the PRI Initiative has become an international organisation (see [www.unpri.org](http://www.unpri.org)). For a very early example of 'ESG matters' embedded in corporate decisions, see the history of Mr Adriano Olivetti and the Olivetti Company based in Ivrea (Italy), which is now a UNESCO World Heritage Site.

<sup>4</sup> Directive 2014/95/EU.

<sup>5</sup> Directive (EU)2017/828.

<sup>6</sup> Regulation (EU) 2020/852.

<sup>7</sup> The principles of non-maleficence and of beneficence are attributed to Hippocrates of Kos (ca.460 BCE–377 BCE) and have been transposed from the ethic principles of physicians. The EU, on the other hand, adopts the precautionary principle for its environmental policy, as set out in the Treaty on the Functioning of the EU.

<sup>8</sup> This is a general trend, which can vary largely in different sectors or different areas of the world.

<sup>9</sup> Plan presented on 11 December 2019 by the European Commission to make Europe the first carbon neutral continent by 2050.

<sup>10</sup> European Commission, Inception Impact Assessment Ref. Ares(2020)4034032-30/07/2020.

<sup>11</sup> European Parliament resolution of 17 December 2020 on sustainable corporate governance (2020/2137(INI)).

<sup>12</sup> The Enacting Purpose Initiative, 2021, by the University of Oxford, Berkeley Law, BCG BrightHouse, Federated Hermes EOS and The British Academy is one of the most recent projects relating to company's purpose.

<sup>13</sup> G20/OECD, *Principles of Corporate Governance*, 2015: 'Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined.'

<sup>14</sup> Lipton, M., Rosenbaum, S., Savitt, W. and Cain, K., 'On the Purpose of the Corporation', WLRK Memo, 26 May 2020.

<sup>15</sup> It seems that the term was first created for the mineral exploration and mining industry, almost 20 years ago.

<sup>16</sup> The China Securities Regulatory Commission published on 28 June 2021 an amended version of disclosure rules which strengthens the requirements for disclosure in connection with ESG matters and related risks.

<sup>17</sup> The SFWG was started in 2016 as a Sustainable Finance Study Group under China's presidency and was upgraded to the status of a Working Group in 2021 under the Italian presidency. In such respect, I have appreciated the work of Professor Ma Jun, from Tsinghua University, who has been leading China's effort for a greener economy for many years now.

<sup>18</sup> The 'comply or explain' principle was introduced by the Cadbury Report in the United Kingdom in 1992 and was subsequently adopted by several stock exchanges (such as the London Stock Exchange and the Hong Kong Exchange) and also in the EU regulation.



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# Ethics and Corporate Governance in the Digital Age and Challenges for Enterprises

‘Digital technology’ or ‘Industry 4.0 era’ are terms that have been frequently mentioned in recent years. While the world has strongly deployed digital technology, in Vietnam many enterprises are still struggling to sufficiently transform with the desire to remove traditional management methods and catch up with the world trend, that is, the Industry 4.0 era.

The transformation is evident in the supporting industries and services. Enterprises in these fields are gradually transforming their business models and management based on technology to connect enterprises with customers and between business departments. The need to keep up with the increasing demands of customers by transforming has led to a shift in managing each enterprise, which has posed a great challenge for business managers on the journey to find a sufficient governance model that aligns with core values for their own enterprise. Within the scope of this article, the ethical issues associated with the corporate governance model in the process of operating an enterprise in the Industry 4.0 era and the challenges will be discussed.





## Introduction

Throughout the world, the digitisation of business activities has been thoroughly applied by enterprises, but in Vietnam, a developing country, the terms 'digital technology' and 'Industry 4.0' have been used and 'data digitisation' has only appeared in recent years. In fact, while enterprises understand the benefits that digital technology brings, there have not been drastic changes,

and it is only now, under the strong impact of the COVID-19 Pandemic with social distancing policies from the Government, etc., that enterprises have been forced to seriously consider the application of digital technology in business activities (previously, digital technology was applied only to support the needs of users, such as for saving time, reducing travel since enterprises can manage work remotely, quick communication, etc.) and to change the way that they operate and adapt if they are to continue to survive.

Digital technology is understood as the process of transforming from a traditional management model to a digital business model by applying new technologies to business activities from the approach to customers, partners and suppliers to internal management. The recent developments in digital technology (such as artificial intelligence, cloud computing, internet of things, etc.) have been variously used by Vietnam enterprises in business, manufacturing and management.

## Corporate Governance in the Digital Age

Digital technology has been a topic of much discussion at the meetings of Vietnamese authorities in recent years, because associated with digital transformation, the legal foundation also needs to be adjusted for compatibility. Currently, the provisions of Vietnamese law related to transactions and methods of interaction through electronic means have been regulated, but these regulations are scattered through many legal documents, correspond to many relationships, and these regulations currently govern only at the level of electronic transactions.

In recent years, digital technology has been of some interest to enterprises, but only at the level of exploration and implementation for gradual adaptation, and the transformation has mostly been in large enterprises. Currently, enterprises choose step-by-step implementation at each stage in production, progressing to each part of the business. Typically, digital transformation for the production line is especially focused. Through this transformation, governance activities are made simpler, when technology has replaced the large number of workers in charge. For other departments, from administration to business, transforming to apply digital technology is also of interest in relation to the benefits brought by digital technology, especially data creation, processing and storage. Technology helps enterprises to digitise data and to store it on a common platform where they have the ability to extract such information whenever





needed as well as without having to use a lot of space and spend on personnel costs for document storage.

Currently in Vietnam, enterprises, when applying digital technology to internal management, often expect that it will help increase the quality and productivity of employees and save costs, including wages; provide easy access without limitation whereby all data is converted to a digital format, which enterprises can access anywhere and at any time; and improve the information security of the enterprise, whereby the access to data is decentralised for each level of management and each department. Based on these factors, enterprises operating in the field of technology have exploited and built applications to match customer needs.

When integrating into the world economy through commitments on opening up and tax incentives, Vietnam is attracting the attention of many investors as an ideal investment destination. To manage investment activities in Vietnam effectively, especially when the situation with the COVID Pandemic is still complicated and policies to restrict entry have been introduced by the Government, investors have chosen digital technology as a method of corporate governance in Vietnam. Accordingly, the processing and storage of data on a digital technology platform makes it easy for investors to control the situation of business activities in Vietnam and ensure the safety of documents, avoid loss and theft.

In fact, most enterprises participating in the transformation process are aiming to convert documents in the form of paper documents into an encrypted format in files stored on a common platform, thus gradually shifting to the digitisation of documents instead of the traditional form, paper documents. What Vietnamese enterprises receive

when making the transition to a digital technology model is an increase in labour productivity, a reduction in human resources involved in production and a reduction in costs, including personnel and management costs.

To adapt to the trend, legal regulations have recognised the validity of the contents and documents created and stored on the basis of digital technology. The Law on E-transactions 2005 provides:

**Article 10. Formats of data messages**

A data message may be shown in the form of electronic data interchange, electronic documents, e-mails, telegrams, telegraphs, facsimiles and other similar forms.

**Article 11. Legal validity of data messages**

Information in data messages cannot have its legal validity disclaimed for the sole reason that it is expressed in the form of data messages.

Aside from the above general rules, separate regulations in other fields have also recognised the value of electronic data, specifically the Law on Accounting 2015 stipulates:

**Article 17. Electronic records**

1. Electronic records are considered accounting records if they have the contents specified in Article 16 of this Article and are displayed in the form of electronic data, encrypted and not changed during transmission through the computer network or telecommunications network or by a storage device such as magnetic tape, magnetic disc, or payment cards.

And most recently, the new Labor Code that takes effect in 2021 has allowed enterprises to establish labour relations and conduct management via electronic means. With changes in legal policies and incentives for enterprises utilising the 'digital technology' that Vietnam is currently applying, it will be a lever for digital technology in Vietnam to develop and enterprises will be more confident in applying the governance model on the basis of digital technology.

**Business Ethics in the Context of Digital Technology**

Currently, certain industries in Vietnam have regulations on codes of conduct and ethics, but these are just a few regulations that create ethical standards for enterprises

in business activities in general. Corporate governance still has not been developed into a specific standard system to guide business behaviours for enterprises. With the economy on the rise and the interweaving of different cultures, some enterprises put ethics in business and governance as a top priority since it is an investment for the future and for the sustainable development of the business.

In addition to the goal of profit, humanity in business methods, product and service quality performed according to the enterprise's commitment is considered as one of the forms of showing ethics in business when aiming to comply with what the enterprise has committed to. While enterprises carry out profitable business activities, these are not separate from social responsibility, which is understood as not merely charitable activities, but further benefits for consumers and the community. This can be simply understood on the basis of the following:

- The actions and decisions of enterprises are creating disadvantages in terms of health and the material and living environment of the community. Some enterprises in Vietnam have violated this in recent years when trying to achieve their goals, for instance, in order to achieve their goal of reducing waste treatment costs, they have discharged sources of waste into the natural environment. The consequences for enterprises have actually been verified as the user community has boycotted products in the Vietnamese market, which is actually the biggest damage that enterprises might suffer due to the violation of business ethics.
- Another aspect is whether an enterprise's actions in management consider the interests of its employees or not. For instance, when converting the traditional management model to a digital technology model, personnel is reduced to make room for technology machines. The question is, when implementing this transformation, whether the enterprise has complied with the provisions required by the labour law when reducing personnel or not. In terms of Vietnamese culture, Vietnam is a country with an Eastern culture with the spirit of helping and sharing difficulties, as well as a large labour force, so the reality will be seen in the process of transformation to digital technology. The reduction of unnecessary personnel is inevitable and enterprises may have

fully fulfilled the requirements prescribed by law, but in order to harmonise both the situation and reasons, in Vietnam enterprises often choose to negotiate with employees before taking action, even those that are allowed by law. This will reduce disputes and strikes in Vietnam and improve an enterprise's reputation.

- Complying with legal regulations and fulfilling commitments to partners and customers are also matters of business ethics.

Business ethics in each country will have different standards depending on the culture and development level, but in general, business ethics will be evaluated on the basis of profit, which must be associated with responsibility to the social community.

### What are the Challenges for Enterprises in Corporate Governance and Building Ethics?

For corporate governance activities, the occurrence of the COVID-19 Pandemic can be considered as a catalyst to help enterprises in Vietnam clearly recognise the need to transform. However, moving from awareness to action will not be easy for every enterprise when there are still numerous barriers that prevent many enterprises from implementing and completing the transformation process. This comes from:

- The specific transformation of applying digital technology to corporate governance causes disturbances within each enterprise. In fact, when digital transformation means that a part of the personnel will be cut, this will cause panic for all employees of the enterprise.
- Financial resources and costs for the transformation will be more or less dependent on each stage of development, the available technology level, as well as actual demand. For many enterprises this is still a burden.
- There are very few human resources for management in enterprises operating on traditional models today, especially those who have access to and are trained in digital technology, so when implementing digital technology this group of personnel must understand the basic principles of the operating mechanism of each element of software, the value it brings and the needs of the business.

The understanding of digital technology and corporate governance by enterprises is still incomplete, which is reflected in the fact that many enterprises do not clearly understand technology trends related to their industries and the business that enterprises are operating, leading to the reality that they are not really ready to change, access technology, infrastructure systems, change processes or change their way of management and administration to meet technology trends.

Corporate governance in the digital age requires those in management positions to be individuals who are knowledgeable about management activities that will be implemented on a digital technology platform, but in reality their relatable knowledge is not high. Enterprises need to make requirements for management levels to improve management capacity in areas including strategic management, finance, human resources, production and marketing resources (including digital resources). There is no uniformity in the application of technology to all parts of the business, whereby most enterprises can only apply a part of technology to management, using individual software such as accounting, CRM, warehouse, sales, etc., with a lack of connection with each other.

Data governance after transforming is also not currently focused. With the application of digital technology, data is generated in many fields from education, sports, entertainment to healthcare, finance and from basic to strategically important data in each enterprise; however, some enterprises have not yet come up with solutions to preserve, avoid leakage and loss of data, which includes both technology and human aspects. In addition, the data storage platform in Vietnam is not trusted much by enterprises due to their concern about data safety and they prefer looking for partners in a foreign country where there is a stable and secure digital technology environment for storage purposes. However, currently Vietnamese law has introduced several new regulations on cases that require data to be stored in Vietnam. This also causes fear for enterprises when transforming their governance model to digital technology.

In terms of corporate ethics, as discussed above, enterprises that properly implement business ethics are an investment for the future; however, in the current context of Vietnam, to build and maintain business ethics there will be many challenges and difficulties that enterprises must face, some of which are mentioned below:

- The legal system stipulating the standards for ethics of enterprises has not been built into a common system of standards, which leads many enterprises to violate legal regulations and commitments to customers and employees to achieve business profits.
- To ensure business benefits and reduce costs when there is a need to convert the traditional operating model to a digital technology governance model, some enterprises have made mass reductions in personnel without relying on agreements between enterprises and employees as well as non-compliance with labour laws. Currently, the labour law requires enterprises to allocate a new job arrangement plan for employees. In case it is not possible to arrange new jobs, enterprises are allowed to cut back after notifying the competent authority in advance for a certain period of time. However, as mentioned above, some enterprises do not comply with this regulation. The reduction of personnel often occurs at manufacturing enterprises, when automatic machine lines replace human labour and, in some cases, these cuts lead to strikes by employees which causes the opposite effect on the enterprise itself in terms of material damage and reputation.
- The development of digital technology has led to some enterprises disregarding legal regulations to search, copy or steal the data of other enterprises for the purpose of creating their own advantages in the market.

### Solutions For Enterprises

Digital technology is a major reform for every enterprise in governance, so in order to avoid financial waste and prolong the transformation time, enterprises need to first survey their own needs to choose management software suitable for production and business activities. Accordingly, enterprises can consider using overall management software to ensure consistency for the entire enterprise.

Enterprises can implement training for personnel from the management team to the operation team, because not every enterprise has technology-savvy personnel, so organising training for employees plays an important role. Identification of weaknesses to overcome and promote each person's strengths as well as at the same time improving the ability to think critically, stimulates effective



teamwork and equips personnel with the necessary skills required by the 4.0 era.

Enterprises can equip themselves with software solutions. For large enterprises that need to process huge amounts of data, applying traditional methods will cause unnecessary difficulties and errors. Software solutions make working, production, sales, recruitment, etc., processes simpler and more accurate. Software also helps the production process to be automated, saving manpower, labour and time.

Enhancing the role of corporate culture and applying digital technology to help enterprises replace the traditional operating model with a digital-based operating model will have a significant impact on the culture of development and cooperation of Vietnamese enterprises. To catch up with the world in the digital economy, enterprises need to say 'no' to stagnation and slowness and exhibit constant innovation and flexibility in approaching customers.

The organisation of training and learning, in the digital age, is important for enterprises. Besides always updating new technology information, they need to organise training sessions, technology tutorials and software solutions to their personnel.

With ethics in business and management, enterprises, when formulating business strategies, need to consider the common interests of the community, partners, suppliers, customers, employees, product quality, services and the ecological environment. Ensuring business standards with partners also complies with the law. Compliance with these principles also helps enterprises to not violate business ethics and creates a reputation for the business for users as well as partners. In addition, carrying out community-oriented activities (such as protecting the environment, creating jobs for ethnic minorities and, together with the Government, contributing to poverty reduction and social equality programs) is also a way for enterprises to promote and strengthen the brand of their business and to show the business ethics of its businesspeople towards the community in accordance with Vietnamese traditions.

On the part of the Vietnamese Government, in order for the legal foundation to be suitable for the transformation of enterprises, the Law on Cyberinformation Security and the Law on Cybersecurity and guiding documents have

been promulgated to ensure timely data security for enterprises when performing the digital transformation. At the same time, in some relevant meetings, the Government has given general orientation and solutions so that competent agencies can build legal regulations on that basis to suit each business activity related to corporate governance and building ethics in digital technology, specifically:

- to prioritise building and perfecting management mechanisms, policies and legal regulations to keep pace with the digital economy and smart industry;
- to build an information technology infrastructure in a synchronous manner;
- to quickly develop human resources of enterprises and state agencies to meet the requirements of the digital economy; and
- as enterprises are the centre and motivation of new technology development and the application of science and technology, developing digital enterprises has been identified as a central and long-term task to develop the digital economy in Vietnam.

The 4.0 era, with the breakthrough of technology, internet and artificial intelligence, will change production and strongly impact the management activities of enterprises. However, the development speed of digital technology is quite fast, so enterprises are forced to continually update to ensure that the technology applied is also compatible with the version that the world is using. Aside from the opportunity, digital technology will also create many challenges affecting the operation of the business community in general and corporate governance specifically.



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# Transformation of Humble Humanisation into a Good Corporate Citizen

Business is any activity or enterprise that participates in making profits. Competent business executives must be able to make high profits for their business within limited budgets. However, that mindset has led to negative effects in society. This article indicates the transformation of the business practices concept for solving accumulated problems and creating sustainability of living through laws, regulations and innovative business frameworks.



## Introduction

The Industrial Revolution led to prosperity capitalism whereby people put a high value on wealth, operating profit and capital accumulation. That concept seemed like an excellent living evolution, but it has caused incredibly adverse effects. Business practices without ethics have caused several difficulties in society, such as the use of illegal labour, destruction of the environment, deception of customers and corruption. In the 1960s, young people began to call for ethics within business operations in order to live in a better world since people began to realise that only making high profits without social responsibility is not the primary factor in making a business successful and sustainable.

Business ethics (also known as corporate ethics) is a form of applied ethics or professional ethics that examines ethical principles and moral or ethical problems that arise in a business environment. It applies to all aspects of business conduct and is relevant to the conduct of individuals and entire organisations.<sup>1</sup> The concept of business ethics began in the 1960s due to young employees desiring a better business environment and the first step involved issues around the rights of labour. In the 1970s to 1980s, defence contractors and other major industries were riddled by scandal in relation to abuse of labour and heightened environmental concerns. The public pushed to make businesses accountable for ethical shortcomings. The contract between employers and employees was redefined for more protection of labour rights. In the 1990s, there were major concerns about child labour, facilitation payments (bribes) and environmental issues. For example, tobacco companies and junk food manufacturers faced heightened scrutiny and lawsuits were filed against them because of their products that affect the health of customers and others, and oil companies and chemical companies had to contend with increasing public pressure to answer for environmental damage. In the 2000s, the world stepped into the online realm and the problems of cybercrime and privacy issues, for instance identity theft. As a result, businesses faced social and legal pressure to take every measure possible to protect sensitive customer information.<sup>2</sup>

## The Present Status of the Business Ethics Concept

At the worldwide level, the business ethics concept appeared in the ten principles of the UN Global Compact which is an organisation of the United Nations

to encourage businesses and firms to adopt sustainable and socially responsible policies and to report on their implementation. Even if the principles are non-binding and breach of them does not have legal sanctions, they are guidelines for ethical business practices in the areas of human rights, labour, the environment and anti-corruption. Moreover, there are other international organisations supporting this concept, such as the non-binding Guidelines for Multinational Enterprises of the Organisation for Economic Co-operation and Development ('OECD') and the non-binding Guiding Principles on Business and Human Rights of the Office of the High Commissioner for Human Rights ('OHCHR'). They indicated that several countries impelled this concept in the global society. Generally, international organisations release non-binding principles, guidelines or frameworks for advancing and supporting the concept of business ethics, but there are some conventions that are binding international laws, such as the International Covenant on Economic, Social and Cultural Rights ('ICESCR') 1966 of the OHCHR. The ICESCR recognises the rights of work that everyone enjoys favourable conditions of work, including fundamental economic rights. Countries ratifying the Convention are bound to abide by its principles by means of implementing and enforcing internal laws in accordance with the Convention.

In addition to the international level, the concept of business ethics has been enshrined in every field of internal business laws, such as corporate laws, environmental laws, labour laws, etc. Internal laws are the main mechanism to control and appoint appropriate business administration. In 2002, the United States legislated the Sarbanes–Oxley Act (the Corporate and Auditing Accountability, Responsibility, and Transparency Act) to set out reforms and additions in corporate responsibility, increasing criminal punishment, accounting regulation and new protections for shareholders, employees and the public. The US Congress passed this Act to resolve spectacular frauds because of the inadequate oversight of accountants, lack of auditor independence, weak corporate governance procedures, stock analysts' conflicts of interest, inadequate disclosure provisions and grossly inadequate funding of the Securities and Exchange Commission.<sup>3</sup> Singapore enacted the Prevention of Corruption Act 1960 to prevent problems of corruption and impose criminal penalties and the Environmental Protection and Management Act 2002 focusing on the issue of environmental pollution control in the areas

of air, water and noise pollution. In Australia, the Fair Work Act 2009 sets minimum standards and conditions for employees and provides the legal framework for employer-employee relations for the majority of workplaces in Australia.

### Examples of Issues Relating to the Concept of Ethics in Business

The concept of ethical business practices has a very broad meaning. To uphold this concept, business executives should consider the following example issues.

#### Environmental Issues

The environmental crisis is a massive problem at a worldwide level. Humans have intensely destroyed the environment since the beginning of the Industrial Revolution. Excessive chasing of profits by businesses has caused terrible effects on the environment. Recently, there was a huge explosion and fire that destroyed a factory that produced plastic foam and plastic pellets in Thailand. It caused extensive damage to surrounding communities, dangerous chemicals spread to the air approximately 10km from the factory and the people in that area had to evacuate rapidly. In relation to water pollution, there has been wastewater emissions into rivers more than 400,000 times by water companies in 2020, sewage caused decreasing oxygen in water which may cause the mortality of aquatic creatures and damaged the water supplies of riverbank communities.<sup>4</sup> These examples are reasons why environmental issues relate to ethical business practices. Attending to these matters and addressing them as urgent problems, governments of many countries have enacted laws/regulations aimed at controlling the operation of businesses which may cause harm to the environment, including preparing an environmental impact assessment ('EIA') before establishing companies. In 1980, the United States adopted the Comprehensive Environmental Response, Compensation, and Liability Act for imposing liability and punishment for industries destroying the environment by creating a tax on the chemical and petroleum industries and providing broad federal authority to respond directly to releases or threatening releases of hazardous substances that may endanger public health or the environment.<sup>5</sup> In 1999, Australia legislated the Environment Protection and Biodiversity Conservation Act to provide for the protection of the environment, especially matters of national environmental significance, by specifying that where an action has, will have, or is likely to have, a significant impact on certain

aspects of the environment, then the approval of the Australian Government Department of the Environment Minister should be requested.<sup>6</sup>

In Thailand, there are many environmental Acts regulating businesses harming the environment, such as the Factory Act (B.E. 2535), the Enhancement and Conservation of National Environmental Quality Act (B.E. 2535), the Public Health Act (B.E. 2535), the Hazardous Substance Act (B.E. 2535), etc. They set the methods of requesting permission to institute business organisations, preparing an EIA, obligations to prevent and protect the environment and punishment and remedies for business' infractions of public health.

#### Human Rights Issues

Human rights has become a big factor driving the transformation of business operations. This issue is directly related to labour, workers and employees. Before transforming the business operations, entrepreneurs focused on their own interests and wealth and treated their labour force as machines, including violating their rights. For example, during the Industrial Revolution, factory increases led to further needs of workers. Children were a good source of labour because they could be paid less and were less likely to organise and strike against their pitiable working conditions. Hence, there was a great deal of utilisation of child labour and those children were used as servants and apprentices for little or no pay. They were unable to attend school and were forced to work long hours in miserable working conditions, including crowded and unclean factories, with a lack of safety codes or legislation.<sup>7</sup> That was one of the worst human rights violations by industries. At present, human rights violations in the business environment can be seen more generally because of the difference in bargaining power between employers and employees. Realising problems and trying to resolve them, several countries regulated labour laws/regulations to set minimum standards of labour rights, such the Employment Act (1968) of Singapore and the Fair Labor Standards Act (1938) of the US. The Singapore Employment Act was legislated in 1968 for standardising and regulating the terms and conditions of employment for all employees regardless of their occupations and title. The Act specified various standards such as hours of work, overtime rates, the number of rest days and holidays, retirement benefits and a restriction on the employment of children, etc.<sup>8</sup> The Fair Labor Standards Act ('FLSA') of the US covers public agencies and



businesses engaged in interstate commerce or providing goods and services for commerce. The FLSA provides guidelines on employment status, child labour, hours of work, minimum wages, overtime pay and record-keeping requirements, including penalties for non-compliance that employers who wilfully or repeatedly violate the Act may be penalised up to US\$10,000 per violation and second convictions can impose US\$10,000 and/or up to six months imprisonment.<sup>9</sup>

Thailand also has employment laws for protecting labour rights. Thailand guarantees fundamental labour rights in the Constitution of Thailand regarding working conditions, in income, welfare, social security and other benefits for suitable living matters, adopted Acts and subsidiary laws to thoroughly protect labour. For instance, the Labour Protection Act (B.E. 2541) stipulates general working conditions: hours of work, extra income for overtime, weekly/traditional/annual holidays and the employment of young workers. The Compensation Act (B.E. 2537) stipulates that employees have rights to receive compensation for injury, disability or death from working. The Act on Establishment of Labour Courts and Labour Court Procedure (B.E. 2522) specifies the process of filing labour disputes in the Labour Court in Thailand.



to €123 million between 1999 and 2005.<sup>11</sup> The Siemens bribery scandal was the corruption case of the Siemens Company, the large German electronic firm which had used bribes to win business in countries around the world, such as Bangladesh, Nigeria, Argentina, Israel and China. Before 1999, the bribery of foreign officials was not illegal in Germany and bribes could be deducted as a business expense under the German tax code, but when the German law changed in 1999, Siemens carried on as before. Finally, US and German prosecutions were filed against Siemens, which had to pay more than US\$1.6 billion in fines, penalties and disgorgement of profits, including US\$800 million to the US authorities. This was the largest monetary sanction ever imposed in a case under America's Foreign Corruption Practice Act since it was passed in 1977.<sup>12</sup> Besides the said US Act, there are other anti-corruption laws/regulations of other countries, such as the Egyptian Anti-Bribery Law in the Penal Code of Egypt, the Argentine Criminal Code of Argentina, the Improper Solicitation and Graft Act of South Korea and the Anti-Corruption Law and Anti-Bribery Law of Indonesia. In Thailand, corruption law is contained in section 63 of the Constitution of Thailand and the Penal Code, especially the Securities and Exchange Act (B.E. 2535) aimed at controlling corruption in the stock market.

**Corruption Issues**

Corruption is dishonest behaviour by those in positions of power, such as managers or government officials. Corruption can include giving or accepting bribes or inappropriate gifts, double-dealing, under-the-table transactions, manipulating elections, diverting funds, laundering money and defrauding investors,<sup>10</sup> that will generate negative effects for the company, such as reduced quality of productivity, damaged stability of business, loss of shareholder and investor confidence and damaged reputation to business relations. Therefore, the ethical business concept being so directly concerned with this issue is an effective tool to address it. There have been many cases of corruption, such as the Gürtel Case and Siemens bribery scandal. The Gürtel Case is Spain's largest corruption scandal that involved the payment of bribes between Spanish businessmen and local leaders of the People's Party ('PP'), Spain's major conservative party, in exchange for rigged government contracts. The funds defrauded amounted

**Monopoly Issues**

Rival companies are a disturbing obstacle for the business of some companies, but it is a significant factor for restraining monopolistic business which may cause product prices to be higher, inferior-quality goods, exploitation of customers and less innovation. A monopoly refers to when a specific person or company and its product offerings dominate one sector or industry by the absence of competition. Monopolistic companies are the only provider of a product and control most of the market share or customers for their product. Consumers have no choice and must purchase the goods from the monopoly. Competitors, especially small companies, are not able to enter the market because their production capability is lower than the monopolistic company.<sup>13</sup> Monopolies increase economic inequality, which is a crucial problem and is difficult to address. However, governments have duties to restrict monopolistic business, especially in relation to important

public utilities such as water supplies, electricity and public transportation. In some countries, governments monopolise public utility businesses to control the exploitation of customers and facilitate the public interest. To discourage monopolistic operations and protect consumers, antitrust law was regulated in some countries. The Sherman Antitrust Act was passed by the US Congress in 1890 to prohibit monopolies, promote fair competition among sellers and give consumers options. The Act also laid out specific penalties and fines for violating its rules. In 1914, the United States passed two additional pieces of antitrust legislation, the Clayton Antitrust Act and the Federal Trade Commission, to define unethical business practices: price-fixing and monopolies, upholding various rights of labour and to prevent and eliminate monopolistic business practices.<sup>14</sup> China also has the Anti-Monopoly Law passed in 2007 and its purposes are preventing and restraining monopolistic businesses, protecting fair market competition, safeguarding the interests of consumers and the interests of society.<sup>15</sup>

In Thailand, the restriction of monopoly is reflected in the Trade Competition Act (B.E. 2560) which superseded the prior Trade Competition Act (B.E. 2542). The Act defined the prohibition of monopolistic business practices and laid out penalties for infringement thereof.

### **Transformation of Human Concerns into a Business Code of Conduct**

Nowadays, many companies recognise the ethical business concept and try to apply the concept to develop their organisations. Examples include:

- From the announcement of the Ethisphere Institute,<sup>16</sup> DTGO, located in Thailand, has been recognised as one of the World's Most Ethical Companies in 2021 for the third consecutive year. DTGO is a diversified group established in 1993 and consists of affiliates such as MQDC, a property developer, Dees Supreme, a trading company and DT Design, a holistic architectural design firm. These businesses aim to be ethical and socially responsible through their financial and practical support. Each DTGO company dedicates 2% of its top-line revenue to social and environmental initiatives. DTGO also supports the Buddharaksa Foundation, focused on education; Dhanin Tawee Chearavanont Foundation, for public health; and the Blue Carbon Society, which addresses global climate change.
- 3M has been recognised as one of the World's Most Ethical Companies in 2021 for the eighth consecutive year. 3M has a Code of Conduct which defines core business conduct principles, values and ethical standards for conducting business with integrity. The Code applies to 3M employees and third-party customers and vendors who act on 3M's behalf. It is what makes 3M's reputation as an ethical company among consumers and gives rise to a positive effect on the quality of work.
- Canon, a leader in digital imaging solutions, has been recognised as one of the World's Most Ethical Companies in 2021 for the fourth consecutive year. The Canon group has a Code of Ethics that expresses the commitments and ethical responsibilities taken by everyone working and cooperating with Canon. The Code is concerned with social responsibility by undertaking several initiatives to reduce the environmental impact of their operations and products, such as producing recycled products and working with other organisations and voluntary programs to reduce the environmental impact of their products and operations.
- Another example is the Japanese company named Kao, which has been recognised as one of the World's Most Ethical Companies in 2021 for the 14th straight year in four of its fields of business: Hygiene and Living Care, Health and Beauty Care, Life Care and Cosmetics. Kao emphasises the concept of Integrity in accordance with the requirements of the law and with ethical standards and undertaking sound business activity in an honest and upright manner. Moreover, Kao has formulated a corporate code of conduct—the Kao Business Conduct Guidelines—to be instilled in all Kao Group employees by implementing training in each country and region.

### **The Advantages of Business Ethics**

The concept of business ethics is the opposite of making maximised profit because ethical business practices operate alongside the obligations to comply with laws, such as labour laws, environmental laws, etc. It causes increased costs and it is time consuming to implement the practices. However, companies will also obtain advantages if directors change business schemes to be more upstanding ethically. When a company behaves ethically, besides improving its reputation this can attract

customers to its products and services and sway them towards loyalty. Customers feel better about parting with their money if they know the goods have been produced ethically and responsibly. Employees will feel more comfortable working for such a business since they work for a company that makes a positive impact. The ethical reputation of a business builds the confidence of investors and they will then be more likely to invest in or continue funding the company. Most importantly, it is also better for society overall.<sup>17</sup>

## Conclusion

The concept of business ethics is developing to be a good value-add for better surroundings and environment. Some countries recognise the concept by enacting and releasing accurate economic policies for implementation and encouragement of the concept and some companies have begun to adopt the concept to improve their businesses. At the least, it shows that there is deprecation for out of date business strategies. Especially in the digital age where people can access information easily and companies are pressured to reveal confidential data by governments or customers, companies have to value their reputation more. Therefore, business directors/managers have to adapt themselves to new ways of trading, attracting customers for the long term and creating a sustainable business.

## Notes:

<sup>1</sup> Donald Nordberg, 'The Ethics of Corporate Governance', ResearchGate; available at [www.researchgate.net/publication/47455785](http://www.researchgate.net/publication/47455785) (accessed 14 July 2021).

<sup>2</sup> Greg Depersio, 'How Have Business Ethics Evolved Over Time?', Investopedia; available at [www.investopedia.com/ask/answers/022615/how-have-business-ethics-evolved-over-time.asp](http://www.investopedia.com/ask/answers/022615/how-have-business-ethics-evolved-over-time.asp) (accessed 14 July 2021).

<sup>3</sup> Lucas, Nance (2004), 'Sarbanes Interview', Findarticles.com. Archived from the original on 22 September 2008. Retrieved 27 August 2010.

<sup>4</sup> David Brown, 'Sewage discharged into rivers 400,000 times in 2020', BBC; available at [www.bbc.com/news/science-environment-56590219](http://www.bbc.com/news/science-environment-56590219) (accessed 19 July 2021).

<sup>5</sup> United States Environmental Protection Agency, 'Superfund: CERCLA Overview'; available at [www.epa.gov/superfund/superfund-cercla-overview](http://www.epa.gov/superfund/superfund-cercla-overview) (accessed 19 July 2021).

<sup>6</sup> 'Environmental Management and Your Business', Support for Businesses in Australia; available at [www.business.gov.au/Risk-management/Environmental-impact/Environmental-management-and-your-business](http://www.business.gov.au/Risk-management/Environmental-impact/Environmental-management-and-your-business) (accessed 19 July 2021).

<sup>7</sup> History.com Editors, 'Child Labor', HISTORY; available at [www.history.com/topics/industrial-revolution/child-labor](http://www.history.com/topics/industrial-revolution/child-labor) (accessed 20 July 2021).

<sup>8</sup> 'Enactment of the Employment Act', HISTORYSG; available at <https://eresources.nlb.gov.sg/history/events/73b9f60e-9252-4b7a-9bcc-e91ee59bdba5> (accessed 20 July 2021).

<sup>9</sup> U.S. Department of Labor, 'Wages and the Fair Labor Standards Act'; available at [www.dol.gov/agencies/whd/flsa](http://www.dol.gov/agencies/whd/flsa) (accessed 21 July 2021).

<sup>10</sup> James Chen, 'Corruption', Investopedia; available at [www.investopedia.com/terms/c/corruption.asp](http://www.investopedia.com/terms/c/corruption.asp) (accessed 20 July 2021).

<sup>11</sup> Sam Edwards, 'Spain's Watergate: Inside the Corruption Scandal That Changed a Nation', *The Guardian*; available at [www.theguardian.com/news/2019/mar/01/spain-watergate-corruption-scandal-politics-gurtel-case](http://www.theguardian.com/news/2019/mar/01/spain-watergate-corruption-scandal-politics-gurtel-case) (accessed 21 July 2021).

<sup>12</sup> Bertrand Venard, 'Lessons From the Massive Siemens Corruption Scandal One Decade Later', THE CONVERSATION; available at <https://theconversation.com/lessons-from-the-massive-siemens-corruption-scandal-one-decade-later-108694> (accessed 21 July 2021).

<sup>13</sup> Adam Hayes, 'Monopoly', Investopedia; available at [www.investopedia.com/terms/m/monopoly.asp](http://www.investopedia.com/terms/m/monopoly.asp) (accessed 20 July 2021).

<sup>14</sup> Federal Trade Commission, 'The Antitrust Laws'; available at [www.ftc.gov/tips-advice/competition-guidance/guide-antitrust-laws/antitrust-laws](http://www.ftc.gov/tips-advice/competition-guidance/guide-antitrust-laws/antitrust-laws) (accessed 21 July 2021).

<sup>15</sup> Ministry of Commerce People's Republic of China, 'Anti-monopoly Law of the People's Republic of China'; available at <http://english.mofcom.gov.cn/article/policyrelease/Businessregulations/201303/20130300045909.shtml> (accessed 20 July 2021).

<sup>16</sup> 'Ethisphere Announces the 2021 World's Most Ethical Companies', ETHISPHERE; available at <https://worldsmoethicalcompanies.com/honorees/> (accessed 22 July 2021).

<sup>17</sup> 'Advantages and Disadvantages of Business Ethics in the Real World', Dominion; available at [www.dominionprint.com/advantages-and-disadvantages-of-business-ethics-in-the-real-world/](http://www.dominionprint.com/advantages-and-disadvantages-of-business-ethics-in-the-real-world/) (accessed 22 July 2021).



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# Corporate Governance in the United Arab Emirates: The New Challenges

In the UAE, there is growing focus and emphasis on corporate governance, which is crucial in enhancing the country's position as a global business and financial hub and a top destination for investment. It is therefore important to describe the corporate governance framework in the UAE and how it is applied in the context of companies that operate within its jurisdiction.





## Overview of the UAE Legal Framework of Corporate Governance

It is important to note that, in the UAE, corporate governance is seen from a legal point of view in the framework of the corporation and places most of its focus on the nature of the contractual relationship defining the rights and obligations between/among shareholders, on one hand, and the managers and/or board of directors/managers, on the other hand.

On 2 February 2020, the Chairman of the Securities and Commodities Authority ('SCA') adopted a new corporate governance guidance for public joint stock companies ('PJSCs') under Chairman of SCA Board Decision No (03 R.M.) of 2020 concerning adopting the Corporate Governance Guide for Public Joint Stock Companies ('Corporate Governance Guide') and came into effect on 2 April 2020. The said Corporate Governance Guide repealed and abolished the previous corporate governance rules (Chairman of SCA Board Decision No (7 R.M) of 2016).



The Corporate Governance Guide defines corporate governance as:

... a set of controls and rules that ensure institutional discipline in relationships and management in the company in accordance with international standards and methods through identifying the responsibilities and duties of the board members and the senior executive management of the company, taking into account the protection of the rights of shareholders and stakeholders.

On 27 September 2020, Federal Decree Law No 26 of 2020 on the amendment of certain provisions of the Federal Law No 2 of 2015 on Commercial Companies ('UAE Companies Law') was passed and came into effect on 2 January 2021. Accordingly, the newly adopted Corporate Governance Resolution compliments the amendment introduced in Article 6 of the UAE Companies Law on Corporate Governance, whereby it specifically states:

Article 6. Subject to the Central Bank's requirements regarding the financial establishments/institutions that are subject to its supervision and monitoring, the Minister shall issue the Resolution that regulates the Corporate Governance except for Public Joint Stock Companies regarding which the Board of Directors of the Authority shall issue the relevant Resolution that regulates the Corporate Governance thereof. The Corporate Governance Resolution shall provide for the rules, controls, and provisions to be observed by the companies.

The Board of Directors of a company or its managers; as the case may be, shall be responsible for the implementation of the rules and criteria of governance.

Therefore, corporate governance is constantly evolving especially in the United Arab Emirates. The Corporate Governance Resolution along with the UAE Commercial Companies Law thus keeps up with the innovations and new rules in line with corporate governance global best practices. The recent reforms on corporate governance in the United Arab Emirates not only provides a focus on publicly listed companies but also other entity types such as limited liability companies so as to regulate risk and ensure transparency in the corporate affairs and operations of these companies and strengthens internal governance mechanisms, in particular on board independence and composition.



In this article, we therefore discuss corporate governance for limited liability companies pursuant to the rules, regulations and the UAE Companies Law and how this relates to public joint stock companies ('PJSC') that have definitive rules and regulations for their corporate governance.

### Limited Liability Companies

The UAE Companies Law sets out the relevant obligations of managers and shareholders of a limited liability company ('LLC'). This includes the following:

#### Management or Supervisory Board

The management or supervisory board of an LLC is explained hereunder:

1. *Structure:* An LLC is defined as: (a) a company in which the number of shareholders is not less than two and not more than 50 and each of them shall be liable only to the extent of their share in the capital; and (b) one natural and juridical person whereby the owner of the company's capital may not be held responsible for the company's liabilities except to the extent of the capital as stated in the company's memorandum of association.

The relevant licensing authority imposes a reasonable capital requirement which varies with the nature of the business of the LLC. The UAE Companies Law has been amended to permit 100 per cent foreign ownership of companies incorporated in the UAE on certain economic activities, thus abolishing the requirement of a minimum of 51 per cent local shareholding.

2. *Management:* An LLC is managed by a person called a 'company manager'. A company manager can either be selected from one of the shareholders or from others for a limited or unlimited period as stipulated in the company's memorandum of association or a separate contract. It is also possible for an LLC to have multiple company managers and in such case the shareholders may appoint a management board.

3. *General restrictions or requirements on the identity of manager/s:* There is no restriction on managers of an LLC, but LLCs must have a local shareholder holding of at least 51 per cent of the registered share capital of the company for certain economic activities that do not allow full foreign ownership.

4. *Liabilities of managers:* The manager of an LLC is liable to the company, its shareholders and other third parties for committing any acts of fraud. A manager must also indemnify the company for any losses or expenses incurred as a result of any misuse of powers and for any acts of default with regard to any applicable law, the company's memorandum of association or misadministration.

5. *Appointment of supervisory board:* If an LLC has more than seven shareholders, the provisions of the UAE Companies Law mandate the constitution of a supervisory board of managers, comprised of at least three shareholders of the LLC. However, the UAE Companies Law is silent on the requirement to have independent or non-executive directors in an LLC.

6. *Supervisory board powers:* A supervisory board has powers to inspect the company's books and documents, instruct the managers to submit a report on company's activities, control the budget, annual report and distribution of profits.

7. *Liabilities of the members of the supervisory board:* Members of a supervisory board shall not be liable for the actions of the managers unless they became aware of the default therein and failed to refer to the same in their report to the general assembly. In the absence of the Board, shareholders who are not managers shall have the same rights of supervision associated with the description of the shareholders as provided by law or the company's memorandum of association.

#### Composition and Meetings of the General Assembly

A general assembly composed of all the shareholders must be held annually within four months following the end of the financial year. Irrespective of the number of the shares held by a shareholder, every shareholder shall have the right to attend the general assembly and may delegate another shareholder who is not a manager or any other party that the company's memorandum of association permits to be appointed to represent a shareholder at the general assembly. Every shareholder shall have a number of votes equal to the number of the shares held or represented by such shareholder.

The general assembly meetings may be held via modern technology methods and the shareholders

may remotely attend those meetings and participate in the discussions and voting.

Unless the company's memorandum of association specifies a greater percentage, the general assembly meeting shall be quorate upon being attended by shareholders owning not less than 50 per cent of the company's share capital subject to the provisions of the UAE Companies Law as amended. In case the first general assembly meeting was not quorate, an invitation shall be sent for a second meeting to be held after at least five days, and by no later than 15 days, from the date of the first meeting. The second meeting shall be deemed quorate regardless of the number of attendees unless the company's memorandum of association provides for a specific percentage of the company's share capital to be present at that meeting.

Subject to the provisions of the UAE Companies Law, the decisions of the general assembly shall not be valid unless passed by the majority of the shareholders present in person and those represented at the meeting by proxy unless the company's memorandum of association specifies a greater percentage. In any case, managers are excluded and they are not entitled to represent shareholders at the general assembly.

### **Appointment and/or Dismissal of Company Auditor**

The general assembly of an LLC is required to appoint one or more auditors for a renewable one-year term. The auditor can be dismissed by a shareholders' resolution passed at a general assembly, provided that the chairman of the board or manager of the LLC notifies the competent authority of such dismissal within seven days as per relevant provision of the UAE Companies Law.

As the provisions of public joint stock companies in relation to auditors are applicable, we note that the conditions for appointing the auditor as stipulated for a PJSC are applicable to an LLC's appointed auditor, which provides for auditor rotation, whereby the appointment term of the auditing company may not exceed six consecutive fiscal years from the date

of appointment. In such case, the auditing partner, responsible for the auditing works of the company, shall be replaced after three fiscal years. The same auditing company may be reappointed after the lapse of at least two consecutive years from the expiration date of its appointment.

### **Public Joint Stock Company Provisions Applicable to an LLC**

The UAE Companies Law specifically provides that the provisions applicable to a PJSC shall apply to an LLC to the extent that such provisions suit the nature of LLCs. In addition, the Cabinet shall, based on the Minister's proposal, issue a Resolution containing the provisions to be applied to LLCs in the cases where the provisions applicable to joint stock companies do not suit the nature of limited liability companies without contravening the provisions of the UAE Companies Law. The aforesaid Resolution shall be restricted to the related parties and transactions in relation to limited liability companies.

Accordingly, below we will discuss in general the special provisions in relation to the corporate governance of PJSCs as provided by the UAE Companies Law and other regulations.

### **Board Committees**

There is no requirement for LLCs to have board committees, unlike with a PJSC, the UAE Companies Law and other regulations make it explicit that such formation of committees and appointment of members are mandatory. Said committees in a PJSC shall be accountable to the Board for its activities. These committees include:

1. *Control Committee and Executive Committee:* The Control Committee shall undertake supervising the Executive Committee. It also undertakes the appointment and dismissal of members of the Executive Committee. The Executive Committee shall undertake daily management of the company, develop and implement the company strategy approved by the Control Committee and implement the risk management framework approved by the Control Committee.

**There is no requirement for LLCs to have board committees, unlike with a PJSC.**

2. *Nomination and Remuneration Committee and Audit Committee:* The Board shall establish a Nomination and Remuneration Committee and an Audit committee. Each committee shall comprise not less than three non-executive board members, two of which must be independent. Each committee must be chaired by an independent board member. The Nomination and Remuneration Committee prepares policies relating to the remuneration, benefits and incentives of the Board and the PJSC's employees. The Audit Committee reviews the financial and audit policies and regulations of the PJSC and works closely with the external auditor of the PJSC to ensure that it carries out its engagement in accordance with applicable law.
3. *Risk Committee and Technology Committee:* In addition, the new rules encourage the establishment of two non-mandatory committees, a Risk Committee and a Technology Committee. The Risk Committee sets out the risk management strategy of the PJSC and the implementation of such policy. The Technology Committee will review and approve the PJSC's technology plans and strategy and ensure the implementation of such plans and strategy.

### **Internal Audit and Compliance Officer**

According to the Corporate Governance Guide, each PJSC must develop an internal audit system and have a specific department in charge of its implementation. This manages and assists the implementation of the PJSC's corporate governance rules in an efficient and effective manner. Each PJSC must also appoint a compliance officer who monitors compliance by the PJSC and its employees with applicable laws and regulations as well as their compliance with the PJSC's own constitutional documents.

### **External Auditing**

Pursuant to the new rules, a PJSC must have an external auditor who is an impartial and independent person. The auditor must be registered with the SCA. The auditor audits the PJSC's activities and examines its administrative and financial regulations and internal audit functions to ensure their effectiveness and appropriateness to the PJSC. The auditor also reviews the PJSC's financial statements and confirms the existence of its assets. The auditor is required to report any non-compliance with relevant laws to the SCA.

### **Related Party Transactions**

The new rules contain restrictions on transactions between a PJSC and its related parties. Any transaction with a related party that does not exceed in value five per cent of the share capital of the PJSC must have the prior approval of the Board. Where such deals are of a value exceeding five per cent of the share capital of the PJSC, the general assembly's approval is required. The related party may not vote with regards to either approval.

Where the value of the transaction exceeds five per cent of the share capital of the PJSC, a valuation by an SCA approved valuer is required. Following such valuation, the transaction must be approved by the general assembly through an ordinary resolution.

Any related party transaction must be disclosed to the SCA together with a confirmation that the transaction is at arms-length and in the interests of the PJSC's shareholders.

The prohibition on related party transactions ('RPT') are also disappplied for LLCs.

### **Disclosure and Transparency**

At the annual meeting of the general assembly, the shareholders hear and endorse the report of the Board of Directors on the activities and financial position of the company during the year and the report of the auditor. Further, the report of the auditor must also be read to the general assembly, and each shareholder will have the right to discuss the report and request clarifications on the facts appearing in the report.

The shareholders are not generally entitled to information about the company's business outside of the general assembly. A shareholder can review the minutes of the general assembly.

The Board is required to set the policies and procedures related to disclosure according to disclosure requirements stipulated.

The company is required to submit an annual corporate governance report, signed by the chairman in accordance with the form prepared by the SCA. Within the corporate governance report, the directors must include a report on risk management and internal controls. The Board of Directors must make this report available to all of the shareholders before submitting

a request to the SCA for approval for conducting the annual meeting of the general assembly.

### Duties and Responsibilities of the Board of Directors

The Articles of Association of the PJSC shall determine the duties and responsibilities of the Board which the Board of Directors has to perform, either collectively or individually. The Corporate Governance Rules set out the minimum corporate governance standards required of a PJSC. The constitutional documents of the relevant PJSC may impose higher standards.

While dealing with unprecedented circumstances such as the COVID-19 Pandemic, directors should continue to act in compliance with their obligations determined by the law as well as any other specific obligations set out in the company's constitutional documents and a failure to properly act can result in personal liability for the directors.

### Recent Regulations

One of the growing trends is geared toward an increase in corporate transparency. The UAE has mandated that all registered entities disclose and report activities being carried out and details of their ultimate beneficial ownership. This is primarily to adhere to international standards in combatting money laundering, corruption and other financial crimes. These regulations include:

1. *Economic Substance Regulations ('ESR')*: In April 2019, the ESR were introduced as part of the UAE's commitment as a member of the OECD Inclusive Framework and in response to an assessment of the UAE's tax framework by the European Union Code of Conduct Group on Business Taxation. The scope of the ESR requires that where the 'Licensee earns income from a Relevant Activity, they must have Economic Substance in UAE and they need to satisfy Economic Substance Test, notify and report to relevant authority'.

In an effort to address the disruption caused by COVID-19 as it may affect the mobility of individuals (due to travel restrictions, self-isolation situations or quarantine requirements), the UAE will take into consideration the impact of COVID-19 on usual operations of companies when making a determination of whether or not a company has demonstrated sufficient economic substance in the UAE.

2. *Ultimate Beneficial Owner Regulations ('UBO')*: In August 2020, all entities licensed in the UAE are required to disclose their beneficial owners to the relevant authority for the purposes of contributing to the development of the business environment in the UAE and its economic position in accordance with the international requirements by regulating the minimum obligations of the registrar and entities established in the UAE, including the licensing or registration procedures, regulating the UBO Register and Shareholders Register and developing effective and sustainable executive and regulatory mechanisms and procedures for beneficial owner data.

### Conclusion

The corporate governance framework in the UAE strongly covers most of the companies that drive its economic growth. Both limited liability companies and public joint stock companies must apply and comply with laws, regulations and best practices to demonstrate the alignment of shareholder, board and management interests in the company in line with the overall objectives of the UAE in developing and promoting a thriving business environment.

The primary corporate governance mechanisms are clearly defined for both LLCs and PJSCs and continue to be reinforced and supplemented with key regulations that promote transparency and adherence to international standards and multi-lateral commitments. Therefore, implementation and compliance are crucial going forward to ensure that companies do their part in further enhancing the UAE's premier position as the place to do business.




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# Corporate Governance and Ethics: A New Challenge to Corporate Governance



Good corporate governance and ethics can serve as guidelines for company directors to perform their duties, administer organisations and create values and a culture to achieve long-term and sustainable desired results.

Corporate governance and ethics are of pivotal importance to both public and private companies worldwide insofar as operations, adaptation to black-swan events, value creation and anticorruption, among other things, are concerned. For the private sector, its implementation is a challenge for companies and their directors, that is, to raise awareness among staff, instil determination and leadership and assess the barometric readings of corporate governance and ethics to achieve long-term sustainability.

This article will discuss corporate governance and ethical issues and the role of the corporate boardroom to create an organisational culture that can materialise an effective regime of corporate governance and ethics.



## Corporate Governance and Ethics

The corporate governance concept is variously defined and the most cited definition has come from the United Nations, which covers eight key characteristics, that is: participatory, consensus-oriented, accountable, transparent, responsive, effective and efficient, equitable and inclusive, and follows the rule of law. Yet, at their crux, they are all principles and methods by which companies are governed in order to promote values, sustainability and to be good corporate citizens. Interlacing with ethics, ethical corporate governance can refer to values and behaviours, processes, procedures and culture, to

achieve the highest standards of effective performance and satisfaction of stakeholders.

It is important for companies and their directors to be responsible for creating mechanisms to ensure that decision-making, organisational operations and their employees are on the same plateau to create positive corporate values and cope with ever-changing and disruptive business environments.

Thailand's public and private sectors have been emphasising corporate governance and ethics since the so-called 1997 'Tom Yum Kung' crisis. In the early 2000s, the Government introduced the concept of good governance into administrative law, which includes rules of law, transparency, participation, accountability, virtues and worthiness. The current Constitution of the Kingdom of Thailand B.E. 2560 (2017), likewise, also emphasises corporate governance and ethics at the national level to achieve continued and sustainable growth and development.

The private sector is also fully aware of the importance of good corporate governance. Although there is no statutory law on corporate governance and ethics, a number of companies, particularly those governed by securities and exchange regulators, have been implementing higher standards of good corporate governance.

### Overall Challenges to Corporate Governance

As goods and services, and even our money, are increasingly digitised, corporate governance and ethics are under increasing challenges. The key challenge is creating an effective ethical corporate governance framework, that is, raising awareness of corporate governance and ethics among corporate and individual citizens and creating mechanisms that could serve as values and drivers of a positive culture. Fundamental questions are: 'Do we need a corporate governance regulatory framework and regulatory agency with enforcement power?'; 'How do we minimise corrupt practices?' and 'How can the boardroom instil corporate governance in their human resources at the individual level?'

### Challenges to Corporate Governance and Ethics in Thailand

Thai business operators are now aware and alert to good corporate governance and ethics. Yet, actual



implementation of the principle, beyond lip service, is yet to be monitored and developed. Common challenges among Thai companies with respect to corporate governance are discussed below.

### **Lack of Understanding of 'Corporate Governance'**

Thai companies did not develop a standard for corporate governance and ethics themselves. Companies adopted the concept and principle from developed countries, most of which have different cultures and, at that time, Thai companies adopted principles of corporate governance but did not have a process for effective implementation.

### **Ethics Versus Nepotism**

In principle, corporate governance is intended to regulate and control director accountability and balance the interests among stakeholders, directors, employees, suppliers/ customers, creditors, communities, etc. However, as we all know, Thais, by culture and custom, have a strong family orientation. Thai company management or company directors provide obvious favours to relatives, and friends in the form of benefits and jobs, in other words, nepotism. Such practices sadly ignore corporate governance and ethics, leading to deterioration of corporate governance and sustainable growth.

### **Corruption**

Corruption is one of the major challenges to corporate governance in Thailand. During my years of legal practice, I have often encountered the notion that companies should offer gifts to government or public officials, including corporate peers, to acquire needed permissions or commercial contracts. In the absence of such gifting and generosity, companies would not secure anything. Therefore, companies are at times at a crossroad as to whether to adhere to their own principles of corporate governance or turn a blind eye to their own value system for immediate gain.

### **Drastic Improvement of Technology**

Technology has become one of the key factors to the effectiveness of corporate governance and ethics. As we are all aware, technology has made all endeavours more convenient, yet deceptively more complex.

While technology can create a boon for companies, it can also inflict a bane. For example, it can create false information and decrease the accountability of companies, as everyone becomes a reporter with his/ her own channel. This is yet to include cyber security risks. Companies are having difficulty regulating and controlling these nuances. It is hence one of the challenges that boardrooms and companies must control in the context of good corporate governance.

### **Thoughts on Increasing the Effectiveness of Corporate Governance and Ethics**

Companies may consider the following thoughts and processes to enhance their corporate governance framework:

#### **Good Corporate Guidelines for Boards of Directors and Organisational Culture**

To achieve such an effective culture, the boardroom has a crucial role to ensure that corporate governance fosters sustainable business values while instilling confidence among its investors.

It is important for a company to have guidelines for its Board of Directors and establish an organisational culture.

It is important for a company to have guidelines for its Board of Directors and establish an organisational culture (that is, behaviour and values jointly forged by people in an organisation, inherited from generation to generation). As seen from a number of publicly listed companies and century-old companies, such guidelines and an effective organisational culture are regarded as valuable organisational assets as they drive and enhance an entity's business towards overall success to enable competitive advantage and long-term growth.

The guidelines should define the role of the Board of Directors based on three primary principles, namely: understanding and values; acting in an exemplary manner and corporate governance for positive development; and preservation of organisational culture for growth and sustainable business operations.

The guidelines should also require that a Board of Directors be aware of its roles and responsibilities as a leader of the organisation. It can do so by creating sustainable values, setting objectives for sustainability, improving its own efficacy, promoting innovation and responsible business conduct and ensuring appropriate risk management and internal control systems. This will

result in positive performance of the business, successful adaptation to shifting business conditions and good relations with markets and the public, all of which are essential to ensure that an entity can grow and survive in the long run.

Simultaneously, the boardroom must ensure that its corporate governance regime develops healthy competition, while taking into account long-term effects and other factors, including ethical business operations, a respect for the rights and duties of its shareholders or stakeholders, societal benefits, environmental consciousness and an ability to adapt to factors causing change.

### Importance and Determination of Organisational Culture

Organisational culture plays a significant role in framing organisational behaviour by employing core values, perspectives, strategies and incentives. The right and appropriate culture would smoothly and successfully drive an organisation to the designated goal. Thus, the boardroom must realise this point and be aware that it has a pivotal role and the leading position to create and drive organisational culture.

### Procedure in Determining Organisational Culture

A boardroom should assess the following guidelines in order to determine organisational culture:

1. Set the parameters of the intended organisational culture by considering internal factors, such as an existing culture, direction and employee structure, together with the external factors such as business environment, technological advances and business models.
2. Conduct research in order to better understand the existing culture and to enhance decision making.
3. Establish a consensus for the intended organisational culture and a predetermined strategy to better enable the organisation to achieve its goal.

### Approaches in Corporate Governance to Create Organisational Culture

As mentioned, the boardroom is the key institutional body and leader to create and drive organisational culture. It does so by adhering to ethical standards.



The boardroom should leverage its prominence to exemplify the following:

1. Begin with one's own self: Directors should begin with an effective culture within their own boardroom in order to build out a value system across the organisation.
2. Create effective messaging: The boardroom and management should continuously communicate the agreed values by any means to personnel at all levels for continuous exposure and, ultimately, absorption.
3. Lead by example: The boardroom should individually express the intended organisational culture through both disposition and behaviour.
4. Monitor and assess: The boardroom should adopt a mechanism for ensuring and tracking that a given organisational culture meets expectations and indicate where improvements are possible. Employee behaviour should also be evaluated through a clear, productive and transparent processes. Measurements of performance should be considered based on standards and business ethics. To this extent, the boardroom must ensure it has sufficient resources to conduct such assessments.

### Duties of the Boardroom in Human Resources

The boardroom should create an awareness among personnel that each individual should cooperate in promoting the intended organisational culture. It must



maintain a sustainable and sound recruitment system, fair performance evaluation with commensurate remuneration for achievement and a career path for employees. A work environment consistent with objectives, strategies and successful business models is also essential.

The boardroom should establish an open-door policy of communication so as to build trust and confidence among employees that their opinions and problems are valued and are to be addressed. The boardroom should establish a channel to submit complaints or suggestions (a 'whistleblower policy') and assign relevant managers to hear their problems or concerns that challenge the intended organisational culture.

To share useful employee input about work patterns for the development of organisational culture, the boardroom should participate in providing formal or informal communications to all related parties as appropriate, especially to those associated with operations, for their further sharing.

### **Metrics of Organisational Culture**

The boardroom should frequently monitor and inspect the organisational culture by, among other things, setting agendas and evaluating important information and relevant measurements. These actions can help assess the quality, direction, risks or difficulties that may affect the objectives of the organisation.

In some cases, employee daily culture can be difficult to access. Therefore, the boardroom should monitor based on appropriate sources of information, using both qualitative and quantitative data. The boardroom should also raise inquiries on a regular basis to help create a clear understanding of the true characteristics of the organisational culture.

### **Key Measurements**

The boardroom should understand and monitor measurements based on the available sources of reliable information. In doing so, the boardroom should adopt multiple methods to gather information against a backdrop of good standards intended to influence the organisational culture and the business environment.

The boardroom must trace and manage any problem relating to the organisational culture. Therefore, it should ensure that the measurements are able to effectively

demonstrate matters regarding organisational culture in order for management to prepare the relevant management plan. Relevant parties must delve into the improvement of organisational values and the restructuring of structures, human resources management and corporate governance. In addition, the boardroom should review and assess potential matters regarding organisational culture, observe the changes in the environment and keep track of any potential matter that may occur.

### **Conclusion**

It is widely recognised that corporate governance and ethics are key to sustainable, profitable operations, adaptation to black-swan events, value creation and anticorruption, among other things. It is the challenge of companies and their boardrooms to implement an effective corporate governance and ethical framework that promotes an organisational culture among their staff and stakeholders. The organisation culture should foster awareness, mutual understanding and positive values, and eliminate nepotism and corruption. Technology, although a challenge, can aid and abet this positive transformation.

Companies should also review their corporate governance guidelines and promote professional ethics to determine the appropriate organisational culture. This process would include periodic assessments and score-carding of the implementation of corporate governance. Effective good corporate governance can ensure growth, reform and long-term sustainability in ever-changing business environments.



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# Challenges in Corporate Governance in India Post- Pandemic



## Introduction

The COVID-19 Pandemic has thrown up a number of challenges in the functioning of businesses and impacted the working of companies across the globe. This in turn has affected corporate governance of companies worldwide.<sup>1</sup> The Pandemic has also brought into the picture some new challenges with respect to corporate governance like the initiation of virtual meetings, remote governance of the corporate ecosystem, and has increased the importance of corporate social responsibility. Resolving corporate governance challenges has become extremely important for both supporting the recovery of companies from the COVID-19 crisis as well as strengthening their resilience to possible future shocks.<sup>2</sup> Corporate governance is the tool for effective operation of the company, mitigation of risk, compliance with the law, enhancing shareholder value and maintenance of the image of the company during such economic downturn.<sup>3</sup> Thus, this article seeks to discuss various challenges faced by India's corporate governance landscape, the need to combat them post-Pandemic and how to effectively counter these diverse challenges by looking at the legal framework of other countries.

This article seeks to provide an overview of issues with respect to separation of ownership and management, board composition, compliance with corporate social responsibility ('CSR') policies and the risk of fraud. Further,

these corporate governance issues are not peculiar to India but are replicated across countries. Thus, it will be interesting for other countries to learn from these challenges and take back plausible solutions.

## Separation of Ownership and Management Challenges

The main challenge for companies is centred around optimisation of functioning and leadership to effectively accommodate the interests of all stakeholders. This issue of separation of management and ownership has been ever-present but has become even more important since the Pandemic. It has become difficult to remotely monitor the influence of the owner-shareholders on management decisions and to ensure these decisions result in balanced outcomes during these unprecedented times. This issue is particularly faced with respect to family-owned companies and Indian companies having concentrated shareholding patterns, which is discussed further below.

## Family-owned Companies

In a study conducted by the National Stock Exchange regarding family-owned companies, it has been observed that it is largely the extent of control exercised by the family that determines performance and profitability of the firm.<sup>4</sup> Although these businesses are facing negative impacts of the Pandemic, their concerns

largely revolve around short-term revenue rather than long-term survival as compared to other companies with dispersed ownership structures. Interestingly, it has been observed in the USA that family businesses are experiencing the Pandemic in a manner different from other businesses<sup>5</sup> due to the intricate relationship between the family members. Thus, it becomes even more important for family-owned companies to separate their ownership from management for effective functioning of these companies and to be able to combat the crisis. One plausible way in which separation of ownership and management can be achieved is by the family members holding non-executive positions on the board and entrusting the management to professionally qualified managers.<sup>6</sup>

### **Concentrated Shareholding**

A concentrated shareholding pattern has been one of the primary features of Indian companies for a very long time.<sup>7</sup> As a result of the majority shares being held by promoters, the agency problems are reinforced and there often exists conflicting interests between the shareholders and management. In the situation of the Pandemic, these were characterised by, *inter alia*, the dilemma reflected in the equity of returning cash to shareholders when the employees were being increasingly laid off or when deciding on whether to suspend or reduce dividends.<sup>8</sup> Dividend cuts have been adopted across the world as a measure<sup>9</sup> to meet the challenges thrown up due to the Pandemic. However, such a step may be detrimental to the interest of shareholders and could be potentially ignored where the separation of ownership and management is absent in totality or is extremely limited.

### **Position of Minority Shareholders**

The Pandemic has created communication problems due to the virtual shift in operations often causing unavailability, personal issues, network issues and so on. In such a virtual scenario, minority shareholders may not be able to effectively counter oppression by the majority. The precarious position of minority shareholders with majority shareholders acting as shadow directors is further evidenced by the controversial Tata-Mistry case.<sup>10</sup> In the said case<sup>11</sup>, holding in favour of Tata Sons, the Supreme Court of India clarified that minority shareholders were not automatically entitled to a seat on a private company's board, absent any statutory provision to that effect. This decision has ramifications for minority shareholders at large who may now have to agree with the majority

shareholders and promoters to get such rights (a board seat) expressly incorporated in the Articles of Association of the company.<sup>12</sup> Considering this, negotiating with the promoters during the Pandemic would be even more problematic because of the communication and coordination problems highlighted above.

### **Addressing the Problems**

In order to address the challenges posed due to the ownership structure of most Indian companies—either largely family-owned or characterised by excessive promoter control—provisions mandating separation of management and ownership in all companies is the need of the hour. If the management is separated from ownership, shareholders would be better placed to hold the directors of the company liable for decisions. It is also more likely that the interest of all stakeholders would be taken into account, ensuring effective human capital management ('HCM'). In this regard, the Pandemic has heightened the demand for disclosure of HCM data like employee turnover, safety incidents, gender pay gap and so on, as disclosed in USA and Canada.<sup>13</sup> Such disclosures could help the shareholders in holding the management responsible and accountable.

### **Board Composition**

#### **Challenges & Plausible Solutions**

Like the previous issue, challenges relating to the composition of the board in terms of gender diversity, types of directors (independent, non-executive, nominee) have also been largely present in the Indian corporate governance context. The increased focus on diversity, equity and inclusion ('DE&I') in corporate boards across the globe, makes it even more important for Indian companies to pay heed to such issues to be at par with multi-national companies. However, the Pandemic has posed some unique challenges when it comes to ensuring gender diversity among boards of directors.

### **Gender Diversity**

In a bid to ensure gender diversity, Proviso 2 of Section 149(1)(b) of the Companies Act 2013 ('the Act') read with Rule 3 of the Companies (Appointment and Qualification of Directors) Rules 2014 makes it mandatory for '(a) every listed company and (b) every other public company having paid-up share capital of one hundred crore rupees or more; or turnover of three hundred crore rupees or more to have at least one woman director on its board of directors'.<sup>14</sup> Further, the

Securities and Exchange Board of India ('SEBI'), vide clause 49 of Listing Agreement relating to Corporate Governance, made having one woman director compulsory from October 2014 onwards.<sup>15</sup> International commitments and the equality provisions in the Constitution of India also justify appointment of women on corporate boards. Despite such provisions, the lack of adequate female representation on corporate boards is a glaring issue. This is further amplified because of the large number of family-owned companies in India which tend to circumvent the female director mandate by appointing someone from the family on the board.

In order to have meaningful representation on the board, it is essential to begin at the grass-roots level since it is these women, appointed at the lower levels, who go on to become members of the board. However, the Pandemic, having put in place a 'work from home' system, has made it even more challenging for women to balance work and home, as a result of which women are exiting the workforce.<sup>16</sup> This in turn is affecting the presence of women at higher positions like on corporate boards. In the USA, for instance, up to two million women (mothers in particular) are considering leaving the workforce or downshifting their careers.<sup>17</sup> To address this issue, in addition to having a mandate of appointing women at the highest echelons, there have to be codified requirements of providing a flexible work environment to women and in fact employing women in the first place. This is especially true in the case of public sector companies that tend to have very little female intake at the entry level itself.<sup>18</sup>

Gender diversity has received attention from countries across the globe, including the USA and Canada, Brazil, the UK, Australia, Japan and Singapore.<sup>19</sup> The steps taken by these countries can serve as potential takeaways for India. In Brazil, the Institutional Shareholders Services, a proxy voting advisory institution, has included gender diversity and onboarding in its board election policy guidelines. Starting 2022, these guidelines seek to recommend negative votes in the absence of a female director on the board.<sup>20</sup> Some of these countries, like the UK, Japan and Singapore, have pre-determined targets of having a certain percentage of the total board

composition as women.<sup>21</sup> This is something that should be strictly enforced in India as well.

### Independent Directors

The concept of independent directors was brought in by the Kumar Mangalam Committee in 1999 and was hailed as the biggest corporate governance reform.<sup>22</sup> However, the reality has been very different from what was envisaged since promoters and majority shareholders exercise significant control over the appointment and functioning of such directors. The true independence of independent directors has been an area of concern, especially in public sector undertakings ('PSUs'). In an investigation conducted by the Indian Express newspaper under the Right to Information Act, it was found that a large number of independent directors in PSUs had links and affiliations with the ruling party.<sup>23</sup> Further, even in the private sector, retired government officials are preferred to be appointed as independent directors and, in some instances, are appointed even before the mandatory post-retirement cooling period expires.<sup>24</sup>

Another instance of the lack of independence of supposedly independent directors is reflected by the ability of promoters or majority shareholders to easily remove independent directors. The ousting of Nusli Wadia as an independent director in the aforementioned Tata-Mistry case serves testimony to this aspect. Wadia was fired since he stood in favour of Cyrus Mistry (an erstwhile director of Tata Sons) in terms of maintaining chairmanship in the Tata group of companies.<sup>25</sup> This clearly reflects a situation of abuse of power of the promoters and majority shareholders and raises serious doubts about the efficacy of the independent director position itself. In order to strengthen the position of independent directors, SEBI has recently tightened rules (to be effective from 1 January 2022) for both appointment/re-appointment and removal of such directors.<sup>26</sup>

As per these new provisions issued by SEBI, a special resolution is now required for appointment or removal of independent directors, such approval being required at the next annual general meeting or within three months of appointment at an extra-ordinary general meeting, whichever is earlier. In addition, two thirds of the total

A concentrated shareholding pattern has been one of the primary features of Indian companies for a very long time.

members on the audit committee and the nomination and remuneration committee are to be independent directors.<sup>27</sup> Disclosure of a resignation letter and a year-long cooling off period for transition from independent director to executive director in a company has also been mandated.<sup>28</sup> A three-year cooling off period has also been put in place for appointment of employees of promoter group companies and key managerial personnel as independent directors.<sup>29</sup> These changes are aimed at increasing the role of public shareholders, addressing the issues raised on the efficacy of independent directors and ensuring better corporate governance overall.

Independence of boards is an issue that is most prominently manifested in India, although companies in the EU, Japan and Singapore also face this issue; these countries are constantly realising the importance of independent directors and have also seen a rise in number of such appointments vis-à-vis other directors.<sup>30</sup> In Singapore, for instance, starting 2022, Singapore Exchange listing rules will require corporate boards to have at least one third independent directors and directors having served more than nine years on the same board will be subject to a two-tier vote by shareholders on their independence.<sup>31</sup> Japan on the other hand reflects an indirect way out: related-party transactions have been subject to increased scrutiny leading to investors focusing on the importance of appointment of independent directors.<sup>32</sup> Indian regulators could adopt such measures as well.

### Corporate Social Responsibility Compliance

Environmental, social and governance ('ESG') management has emerged as an important consideration globally, warranting compliance with government-mandated standards for the same. This has been amplified by the Pandemic, as the role of companies in ensuring social and economic equity as part of good business practices, has been emphasised and the relation between business and society has been brought to the forefront. The global prediction for 2020 has seen a greater emphasis on the 'E' and 'S' with the growing awareness of climate change, and the Pandemic having forced companies to reassure stakeholders about their commitment to the health and

safety of their workers.<sup>33</sup> In India, CSR is one area that has seen significant development during the Pandemic.

The newly introduced Companies (Corporate Social Responsibility Policy) Amendment Rules 2021 ('New CSR Rules') and the amendments made to Section 135 of the Companies Act 2013 overhaul the CSR framework in India. Owing to the COVID-19 Pandemic, the Ministry of Corporate Affairs ('MCA') permitted consideration of the expenditure of companies to fight the Pandemic (like engaging in healthcare, sanitisation, disaster management and so on) as valid under CSR activities.<sup>34</sup> The MCA has also issued multiple clarifications on what could be considered as CSR expenditure to assist companies in compliance and finalising CSR budgets, especially in light of the second wave of the pandemic in India. As per the New CSR Rules, a greater role of the CSR Committee and the board is envisaged. While the CSR Committee is mandated to formulate an annual action plan for CSR spending, the board steps in for passing resolutions to approve CSR projects and setting off excess CSR funds. In addition, under the New CSR Rules, companies are now permitted to take the assistance of international organisations for designing, evaluating and monitoring their CSR activities.

The New CSR Rules increase governance and transparency of CSR projects owing to the mandate of disclosing the composition of the CSR Committee, the CSR policy of the company and details of the projects undertaken. Since there is a mandatory requirement of impact assessment of CSR projects, governance of the projects at the ground level as well as assisting the independent agency undertaking such impact assessment is required. In addition, the annual disclosures also have to be more detailed requiring monitoring. The excess unspent CSR funds have to be transferred to an 'Unspent CSR Account' and, if not utilised for three years, have to be transferred to any fund specified in Schedule VII of the Companies Act 2013.<sup>35</sup>

These provisions warrant close attention in terms of corporate governance because of the mandatory nature of the obligation and a shift from 'comply or explain' to 'comply or pay penalty'. In case of non-compliance, the defaulting company is liable to payment of monetary

**Corporate fraud and scams represent some of the biggest failures of corporate governance in India and is a continuing issue to this day.**

penalty to the tune of Rs. 1 crore (approximately US\$135,000) or twice the amount that should have been transferred to the unspent CSR account, whichever is lesser. The defaulting officer is also liable pay the lesser of Rs. 2 lakh (approximately US\$2,700) or one tenth of the amount that should have been transferred to the unspent CSR account.<sup>36</sup> From a corporate governance perspective, the New CSR Rules can be seen as an attempt at effective ESG Management, an aspect that has gained substantial attention across the globe during the Pandemic years in particular. India's CSR policies reflect best practices and can serve as an example for other countries in this regard.

### Risk of Fraud

Corporate fraud and scams represent some of the biggest failures of corporate governance in India and is a continuing issue to this day,<sup>37</sup> ranging from the recent ICICI Bank bribery case<sup>38</sup> to the Satyam scam<sup>39</sup> more than a decade ago. In fact, the increased attention to corporate governance was brought after such scams started coming to light. The large amounts of funds involved in these scams make it an extremely grave issue, especially since it is often the hard-earned money of the general public that is at stake. Experts have identified an increase in fraud and corporate misconduct due to Pandemic-induced financial stress as a grave concern, with the 2008 financial crisis serving testimony to the impact of such major disruptive events.<sup>40</sup> The pressure created due to a bad economy, coupled with less oversight due to remote governance, provides fertile ground for operation of fraudsters.<sup>41</sup>

More specific to the challenges thrown up due to the Pandemic, there is a looming fear of revival and recovery being derailed by risks of corruption, bribery and fraud.<sup>42</sup> Employees working from home have been given access to accounting and financial systems from less secure places, such as their homes, making supervisory oversight in a remote manner very difficult and challenging. Also, cybersecurity measures have gained importance owing to the virtual shift in operations. It was found that 38 per cent of organisations in the USA have increased their budget for anti-fraud technology in 2021 and more than 80 per cent have, in response to COVID-19, already made changes to their anti-fraud programs.<sup>43</sup> These are some measures that could be adopted by Indian companies as well.

Further, there has been a heightened demand for transparency in operations, in the interest of privacy and data protection. Corporate communication and disclosures

have significantly changed during the Pandemic. This is not just unique to India, but is instead a global issue. Internal controls are the need of the hour; a strong whistleblower policy protecting bona fide whistleblowers could help check employee-driven fraud and should be considered as an effective pillar of corporate governance.<sup>44</sup> Companies need to be proactive and take steps to first, assess where their vulnerabilities to be a victim to fraud lie; second, institute fraud mitigation procedures (like strengthening the whistleblower policy); and, third, actively monitor red flags.<sup>45</sup>

### Conclusion

The Pandemic has highlighted the importance of corporate governance and posed new challenges in jurisdictions across the world. Having robust corporate governance mechanisms, adopting risk management strategies and identifying the purpose of undertaking business itself have become crucial to combat this crisis. However, corporate governance is not a short-term goal to combat this crisis, but is in fact a long-term goal for the growth of companies. Separation of the management and ownership and ensuring true independence of directors ensures effective management of the company and in turn helps in increasing the valuation of the company. Corporate Social Responsibility helps in contributing to society and building the goodwill of the company. India is on the path of adopting the best corporate governance norms from across the world, however, there is room for ensuring effective implementation. The challenges faced by India with respect to corporate governance are common to many other countries. Thus, there is a need to discuss these challenges together and come up with harmonious solutions for the prosperity of the world economy.

### Notes

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<sup>2</sup> [www.oecd.org/daf/ca/corporate-governance-factbook.pdf](http://www.oecd.org/daf/ca/corporate-governance-factbook.pdf).

<sup>3</sup> *Corporate Governance in India—Why is It So Critical?*, ProSchool (IIM), [www.proschoolonline.com/blog/corporate-governance-india](http://www.proschoolonline.com/blog/corporate-governance-india).

<sup>4</sup> Jayati Sarkar and Ekta Selarka, *Women on Board and Performance of Family Firms: Evidence from India*, NSE India (Oct., 2015), [www1.nseindia.com/research/content/NSE-IGDR-WP6-14-15.pdf](http://www1.nseindia.com/research/content/NSE-IGDR-WP6-14-15.pdf).

<sup>5</sup> Jose Maria Liberti, 'Family Businesses Are Experiencing the COVID-19 Crisis in Unique Ways', *KelloggInsight* (3 September 2020), <https://insight.kellogg.northwestern.edu/article/family-businesses-experiencing-covid-19-crisis>.

<sup>6</sup> S Subramanian & Nupur Pavan Bang, 'How Can Family Businesses Keep Themselves From Splitting? By Separating Ownership and Management', *The Economic Times* (10 March 2021), <https://economictimes.indiatimes.com/news/company/corporate-trends/how-can-family-businesses-keep-themselves-from-splitting-by-separating-ownership-and-management/articleshow/81427776.cms>.



<sup>7</sup> Manoj Pant & Manoranjan Pattanayak, *Insider Ownership and Firm Value: Evidence from Indian Corporate Sector*, 42 EPW 1459, 1459–1467 (2007).

<sup>8</sup> Paine, n 1 above.

<sup>9</sup> P Saravanan, *COVID-19 impact on dividend income: Learning to live with dividend cuts*, Financial Express (18 May 2020), [www.financialexpress.com/money/covid-19-impact-on-dividend-income-learning-to-live-with-dividend-cuts/1962021/](http://www.financialexpress.com/money/covid-19-impact-on-dividend-income-learning-to-live-with-dividend-cuts/1962021/).

<sup>10</sup> The Tata-Mistry dispute arose due to the ousting of Cyrus Mistry as a director of Tata Sons Ltd. Mistry had held the position since 2006 and was a minority shareholder in the company. The majority shares were held by trusts of the Tata family in a bid to retain control. The Board of Directors often disagreed with Mistry's decisions and he was ousted at one such meeting. He challenged this decision and alleged that the Tatas exercised dominant control over the firm and that he was never allowed a free hand to manage the company.

<sup>11</sup> *Tata Consultancy Services Ltd v Cyrus Investments (P) Ltd*, 2021 SCC Online SC 272.

<sup>12</sup> Editorial, *Shining a light*, The Indian Express (1 April 2021), <https://indianexpress.com/article/opinion/editorials/supreme-court-tata-mistry-case-verdict-rights-of-minority-shareholders-7253396/>.

<sup>13</sup> Rusty O'Kelley, Anthony Goodman & Laura Sanderson, *2021 Global and Regional Trends in Corporate Governance*, Harvard Law School Forum on Corporate Governance (3 March 2021), <https://corpgov.law.harvard.edu/2021/03/03/2021-global-and-regional-trends-in-corporate-governance/>.

<sup>14</sup> Companies (Appointment and Qualification of Directors) Rules 2014 (India).

<sup>15</sup> Rica Bhattacharya & Sachin Dave, 'No Independent Woman Director at 40% of NSE Companies', *Economic Times* (9 October 2017), <https://economictimes.indiatimes.com/jobs/no-independent-woman-director-at-40-of-nse-companies/articleshow/61011676.cms?from=mdr>.

<sup>16</sup> Flynn Lebus, Laura Amaya, Sujata Rathi & Harshika Gupta, *Seven Key Issues Affecting Women and Girls During COVID-19 Pandemic—And What You Can Do About Them*, FSG (5 May 2020), [www.fsg.org/blog/seven-key-issues-affecting-women-and-girls-during-covid-19-pandemic](http://www.fsg.org/blog/seven-key-issues-affecting-women-and-girls-during-covid-19-pandemic).

<sup>17</sup> Sarah Coury et al., *Women in the Workplace*, McKinsey (30 September 2020), [www.mckinsey.com/featured-insights/diversity-and-inclusion/women-in-the-workplace#](http://www.mckinsey.com/featured-insights/diversity-and-inclusion/women-in-the-workplace#).

<sup>18</sup> Sutapa Sanyal, *Is the Gender Diversity Gap Narrowing in the Public Sector?*, People Matters (6 February 2019), [www.peoplematters.in/blog/diversity/how-do-you-see-the-gender-diversity-gap-narrowing-in-the-public-sector-20742](http://www.peoplematters.in/blog/diversity/how-do-you-see-the-gender-diversity-gap-narrowing-in-the-public-sector-20742).

<sup>19</sup> O'Kelley, n 13 above.

<sup>20</sup> ISS Brazil, *Proxy Voting Guidelines Benchmark Policy Recommendations*, ISSGovernance.com (2020), [www.issgovernance.com/file/policy/active/americas/Brazil-Voting-Guidelines.pdf](http://www.issgovernance.com/file/policy/active/americas/Brazil-Voting-Guidelines.pdf).

<sup>21</sup> O'Kelley, n 13 above.

<sup>22</sup> Robin, *Corporate Governance in India: Issues and Importance*, IJRAR (2019), [http://ijrar.com/upload\\_issue/ijrar\\_issue\\_20543494.pdf](http://ijrar.com/upload_issue/ijrar_issue_20543494.pdf).

<sup>23</sup> Shyamal Yadav, *How Independent Are Independent Directors of PSUs? Half From BJP*, The Indian Express (2 July 2021), <https://indianexpress.com/article/india/how-independent-are-independent-directors-of-psus-half-from-bjp-7380271/>.

<sup>24</sup> Sandeep Singh, Krishn Kaushik & Pranav Mukul, *Not Just PSUs, Even India Inc Likes IAS On Board as Director*, The Indian Express (2 July 2021), <https://indianexpress.com/article/india/how-independent-are-independent-directors-of-psus-not-just-psus-even-india-inc-likes-ias-on-board-as-director-7383486/>.

<sup>25</sup> Kasmin Fernandes, 'Biggest Corporate Governance Failures in India', *The CSR Journal* (20 April 2021), <https://thecsrjournal.in/corporate-governance-failures-india/>.

<sup>26</sup> Jagadish Shettigar & Pooja Misra, *Why Sebi is Strengthening Independent Directors*, Mint (7 July 2021), [www.livemint.com/market/stock-market-news/what-sebi-giving-a-free-hand-to-directors-means-11625593994324.html](http://www.livemint.com/market/stock-market-news/what-sebi-giving-a-free-hand-to-directors-means-11625593994324.html).

<sup>27</sup> Smiti Chaudhary, *Impact of SEBI Amendments on Norms for Independent Directors*, Money Control (30 June 2021), [www.moneycontrol.com/news/business/markets/explained-impact-of-sebi-amendments-on-norms-for-independent-directors-7105731.html](http://www.moneycontrol.com/news/business/markets/explained-impact-of-sebi-amendments-on-norms-for-independent-directors-7105731.html).

<sup>28</sup> PTI, 'Sebi Approves Stricter Independent Director Norms, Measures to Attract More Investors Into Market', *The Economic Times* (29 June 2021), <https://economictimes.indiatimes.com/markets/stocks/news/sebi-approves-stricter-independent-director-norms-measures-to-attract-more-investors-into-market/articleshow/83964779.cms>.

<sup>29</sup> Chaudhary, n 27 above.

<sup>30</sup> O'Kelley, n 13 above.

<sup>31</sup> *Ibid.*

<sup>32</sup> *Ibid.*

<sup>33</sup> *Ibid.*

<sup>34</sup> <https://egazette.nic.in/WriteReadData/2021/224640.pdf>.

<sup>35</sup> The Companies Act 2013, No. 18, Acts of Parliament, 2013 (India).

<sup>36</sup> Samheeta Rao, 'CSR Act Amendments: All You Need to Know', *The Times of India* (30 April 2021), <https://timesofindia.indiatimes.com/blogs/developing-contemporary-india/csr-act-amendments-all-you-need-to-know/>.

<sup>37</sup> Fernandes, n 25 above.

<sup>38</sup> The ICICI Bank-Videocon money laundering case involved an Enforcement Directorate probe into a Rs. 1875 crore loan given by the Bank to the Videocon group. It was revealed that Venugopal Dhoot (Videocon group chairman) and Deepak Kochhar (husband of former ICICI Bank managing director Chanda Kochhar) had appointed their office boys and junior employees, drivers and gardeners as dummy directors in their group companies. Further, it was alleged that ICICI Bank sanctioned various high value loans in blatant violation of the rules and policies of the sanctioning committee. See Neeraj Chauhan, 'ICICI Bank Fraud: Drivers, Gardeners Were Directors in Deepak Kochhar and Dhoot's Companies, They Didn't Know, Says ED', *Hindustan Times* (9 December 2020), [www.hindustantimes.com/india-news/icici-bank-fraud-deepak-kochhar-s-driver-office-boy-and-gardener-were-dummy-directors-says-ed/story-OLi1BANyIUs3sSFna5BL.html](http://www.hindustantimes.com/india-news/icici-bank-fraud-deepak-kochhar-s-driver-office-boy-and-gardener-were-dummy-directors-says-ed/story-OLi1BANyIUs3sSFna5BL.html).

<sup>39</sup> Satyam, a reputed public listed company in India colluded with auditors and engaged in accounting fraud to mislead various stakeholders, including the investors, the Board and regulators. The fraud came to light upon the company's chairman, Mr Ramalinga Raju, confessing to the malpractices and misrepresentations. Subsequently, the SEBI and other regulatory bodies took action against the company. Post this, a number of corporate governance aspects like shareholders rights, policy governing audit committees, whistleblower policy and so on were reviewed. See Fernandes, n 25 above.

<sup>40</sup> Gireesh Chandra Prasad, *Pandemic May Trigger Rise in Corporate Fraud, Warn Experts*, Mint (11 February 2021), [www.livemint.com/news/india/pandemic-may-trigger-rise-in-corporate-fraud-warn-experts-11613066872850.html](http://www.livemint.com/news/india/pandemic-may-trigger-rise-in-corporate-fraud-warn-experts-11613066872850.html).

<sup>41</sup> Geoff Colvin, 'The Pandemic May be the Greatest Environment for Business Fraud in Decades', *Fortune* (12 November 2020), <https://fortune.com/2020/11/12/pandemic-corporate-fraud-scams/>.

<sup>42</sup> Sachin Dave, 'Companies See Corporate Governance, Frauds as Major Issues in Post-Covid World', *The Economic Times* (26 February 2021), <https://economictimes.indiatimes.com/news/company/corporate-trends/cos-see-corporate-governance-frauds-as-major-issues-in-post-covid-world/articleshow/81216301.cms>.

<sup>43</sup> Michael Cohn, *Fraud Likely to Increase Post-pandemic*, Accounting Today (21 June 2021), <https://www.accountingtoday.com/news/fraud-likely-to-increase-post-pandemic>.

<sup>44</sup> Prasad, n 40 above.

<sup>45</sup> Nelson Luis, *A Blueprint to Managing Corporate Fraud Risk During a Pandemic*, EisnerAmper (13 July 2020), [www.eisneramper.com/corporate-fraud-risk-covid-19-flvs-blog-0720/](http://www.eisneramper.com/corporate-fraud-risk-covid-19-flvs-blog-0720/).



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- ◆ Commercial Contracts
- ◆ Corporate and Securities Laws
- ◆ Corporate Insolvency and Restructuring
- ◆ Dispute Resolution - Arbitration and Litigation
- ◆ Energy, Oil and Gas
- ◆ Environment
- ◆ Employment and Industrial Relations
- ◆ Foreign Investment and Exchange Control
- ◆ Infrastructure and Project Finance
- ◆ Intellectual Property
- ◆ International Trade
- ◆ Information Technology & Outsourcing
- ◆ Insurance
- ◆ Joint Ventures, Foreign and Technical Collaborations
- ◆ Legal Compliance, Bribery & Anti-Corruption
- ◆ Mergers and Acquisitions
- ◆ Mining and Resources
- ◆ Private Equity and Funds
- ◆ Procurement and Transaction Advisory
- ◆ Real Estate
- ◆ Regulatory Affairs
- ◆ Taxation
- ◆ TMT