

Paper-6: LAWS, ETHICS AND GOVERNANCE

Full Marks: 100

Time Allowed: 3 Hours

This paper contains 3 questions. All questions are compulsory, subject to instructions provided against each question. All workings must form part of your answer. Assumptions, if any, must be clearly indicated.

Question 1: Answer all questions

2 X 10 = 20

- (i) A offered to purchase shares of XYZ Ltd on 1st May 2014. The company made allotment of shares on 30th November 2014. A refused to accept the shares. Can it do so?
- (ii) Ascertain the date of maturity of a bill payable hundred days after sight and which is presented for sight on 4th September, 2014.
- (iii) X is engaged in two types of job in a factory, that of a mechanic and watchman. The wage rates are different for two different jobs. The employer calculates his minimum wage at an average rate. State whether this is correct as per the Minimum Wages Act, 1948?
- (iv) The payment of contribution to provident fund of an employee, to be made by his employer, who has become insolvent. A preferential payment as per the provisions of the Employees Provident fund and Miscellaneous Provisions Act, 1952 is possible?
- (v) A contracts to sell B, by showing sample, certain quantity of lotion described as "Imported". The lotion when delivered matches with the sample, but is not "imported" but "Made in India" but of the same company. Referring to the provisions of Sale of Goods Act, 1930 advise the remedy, if any, available to B.
- (vi) When is a LLP not bound by act of its members?
- (vii) State the ethical objectives of a management accountant professional.
- (viii) What aspects should be considered for ethical conflict resolution?
- (ix) "Outsiders are bound to know the constitution of the company and not the indoor management". Justify.
- (x) State whether a promoter has legal right to claim promotional expenses for his services.

Answer:

- (i) According to Sec 6(2) of the Indian Contract Act, 1872 an offer is revoked by lapse of time prescribed in the proposal or by lapse of reasonable time without communication of acceptance. What is reasonable time is question of fact in each case. In the given case the offer lapsed as it was not accepted within reasonable time [Ramsgate Victoria Hotel Co. vs Montefiore.]
- (ii) In this case the day of presentment for sight is to be excluded i.e. 4th September, 2014. The period of 100 days ends on 13th December, 2014 (September 27 days + October 31 days +

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

November 30 days + December 13 days). Three days of grace are to be added. It falls due on 16th December, 2014.

(iii) Where an employee does two or more classes of work to each of which a different minimum rate of wages is applicable, the employer shall pay to such employee in respect of the time respectively occupied in each such class of work, wages at not less than the minimum rate in force in respect of each such class. Thus employer just cannot pay him at simple average rate of both wages of both classes of job.

(iv) According to Section 11 of the Employees Provident Fund and Miscellaneous Provisions Act 1952, if the employer is adjudged as insolvent or if the employer is a company and an order winding thereof has been made, the amount due from the employer whether in respect of the employee's contribution or employer's contribution must be included among the debts which are to be paid in priority to all other debts in the distribution of the property of the insolvent or the assets of the company.

In other words, this payment will be a preferential payment provided the liability thereof has accrued before this order of adjudication or winding up is made.

(v) B has a remedy to repudiate the contract. According to section 15 of the Sale of Goods Act, 1930, when the goods are sold by sample as well as by description, there shall be an implied condition that the goods shall correspond to the sample as well as description. In this case, A supplied lotion which did correspond with the sample but was not correspond to the description of "Imported".

Hence the B has the right to repudiate the contract.

(vi) A limited liability partnership is not bound by any act of a member in dealing with a person if:

- a) The member in fact has no authority to act for the limited liability partnership by doing that thing;
- b) The person knows that the member has no authority or does not know or believe him to be a member of limited partnership.

(vii) Practitioners of management accounting and financial management have a responsibility to:

- A. Communicate information fairly and objectively.
- B. Disclose fully all relevant information that could reasonably be expected to influence an intended user's understanding of the reports, comments, and recommendations presented.

(viii) To resolve the conflict, following aspect should be considered:

- A. Relevant facts;
- B. Ethical issues involved;
- C. Fundamental principles related to the matter in question;
- D. Established internal procedures; and
- E. Alternative courses of action

(ix) The constitution of MOA of the company is a public document and is filed with ROC. Every person dealing with the company is supposed to know its provisions. Indoor management is the internal affairs of the company and it is presumed that the company has complied with the procedural matters. Hence the statement is true.

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

(x) A promoter shall have no legal rights to claim promotional expenses for his services unless there is a valid contract. The promoter needs to make proper disclosure and then he may be rewarded for his services.

Question 2: Answer any 4 questions

4 X 12 = 48

Question 2(a)

(i) X sent a consignment of mobile phones worth ₹60,000 to Y and obtained a railway receipt thereof. Later, he borrowed a loan of ₹40,000 from Star Bank and endorsed the railway receipt in favour of the Bank as security. In transit the consignment of mobile phones was lost. The Bank files a suit against the railway for a claim of ₹60,000, the value of the consignment. The railway contended that the Bank is entitled to recover the amount of loan i.e. ₹40,000 only. Examining the provisions of the Indian Contract Act, 1872, decide, whether the contention of the railway is valid.

(ii) TV is the holder of a bill of exchange made payable to the order of 'P'. The bill of exchange contains the following endorsements in blank:

| | |
|--------------------|-----|
| First endorsement | 'P' |
| Second endorsement | 'Q' |
| Third endorsement | 'R' |
| Fourth endorsement | 'S' |

'N' strikes out, without S's consent, the endorsements by 'Q' and 'R'. Decide with reasons whether 'N' is entitled to recover anything from 'S' under the provisions of Negotiable Instruments Act, 1881.

(iii) S retired from the services of PQR Limited, on 31st March, 2013. He had a sum of ₹5 lakh in his Provident Fund Account. It has become due for payment to S on 30th April, 2013 but the company made the payment of the said amount after one year. S claimed for the payment of interest on due amount at the rate of 15 percent per-annum for one year. Decide, whether the claim of S is tenable under the provisions of the Employee's Provident Funds and Miscellaneous Provisions Act, 1952.

[4+4+4= 12]

Answer:

(i) The given problem is based on the case of Morvi Mercantile Ltd. v Union of India. As stated by the Court, the deposit of title deed with the Bank as security against an advance constitutes a Pledge, as per Sections 178 and 178A of the Indian Contract Act, 1872.

As a Pledgee, a banker's rights are not limited to his interest in the goods pledged. In the case of injury to the goods or their deprivation by a third party, the Pledgee would have all such remedies that the owner of the goods would have against them.

In this case the Supreme Court also held that the Bank (Pledgee) was entitled to recover not only the amount of the advance due to it, but also the full value of the consignment. However, the amount over and above his interest is to be held by him in trust for the Pledger.

Thus, the Star Bank will succeed in recovering the claim of ₹60,000 against the railway.

(ii) According to Section 40 of the Negotiable Instruments Act, 1881, where the holder of a

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

Negotiable Instrument without the consent of the endorser destroys or impairs the endorser's remedy against a prior party the endorser is discharged from liability to the holder to the same extent as if the instrument had been paid at maturity. Therefore if the endorsements of 'R' and 'Q' are struck out without the consent of 'S', 'N' will not be entitled to recover anything from 'S', the reason being that as between 'R' and 'S' 'R' is the principal debtor and 'S' is the surety. If 'R' is released by the holder under Section 39 of the Act, 'S' being surety will be discharged. In this given problem, the rule may be stated thus that when the holder without the consent of the endorser impairs the endorser's remedy against a prior party, the endorser is discharged from liability to the holder.

(iii) According to section 7Q of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 the employer shall be liable to pay simple interest @ of 12% per annum or at such higher rate as may be specified in the Scheme on any amount due from him under this Act from the date on which the amount has become so due till the date of its actual payment: Provided that higher rate of interest specified in the Scheme shall not exceed the lending rate of interest charged by any scheduled bank.

As per above provision, S can claim for the payment of interest on due amount @ 12 percent per annum or at the rate specified in the Scheme, whichever is higher, for one year. Here in the absence of specified rate he(S) can claim only 12 percent per annum interest on the due amount.

Hence claim of S for interest rate of 15% is not tenable.

Question 2(b)

(i) 'A' draws a bill of exchange payable to himself on X', who accepts the bill without consideration just to accommodate 'A'. A transfers the bill to 'P' for good consideration. State the rights of A' and 'P'. Would your answer be different if 'A' transferred the bill to 'P' after maturity?

(ii) Ramesh, aged 16 years, was studying in an engineering college. On 1st March, 2012 he took a loan of ₹1 lakh from Suresh for the payment of his college fee and agreed to pay by 30th May, 2014. Ramesh possesses assets worth ₹10 lakhs. On due date Ramesh fails to pay back the loan to Suresh. Suresh now wants to recover the loan from Ramesh out of his assets. Whether Suresh would succeed? Decide, referring to the Provisions of the Indian Contract Act, 1872.

(iii) Mr. X was serving in Popular Company Limited. After serving for four years X met with an accident and became permanently disabled. X applied to the company for the payment of gratuity. The company refused to pay the gratuity on the ground that X has served only for four years. Decide, whether the contention of the company is valid?

[4+4+4=12]

Answer:

(i) The problem is based on the provisions of sections 43 and 59 of the Negotiable Instruments Act, 1881. 'A' cannot recover from 'X' because it is an accommodation bill drawn by 'A' and accepted by 'X' without consideration. According to section 43, an instrument without consideration creates no obligation between the parties to the transaction i.e. 'A' and 'X' in this case.

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

Section 43 also provides that if such a bill is transferred to a holder for consideration, such holder may recover the amount due on such instrument from the transferor for consideration or any prior party thereto. Hence 'P' in this case can recover the amount from 'X' and 'A'.

According to Section 59, in the case of accommodation bills, a defect in the title of the transferor does not affect the title of holder acquiring after maturity. Hence the answer will be the same even if P' has acquired the bill for consideration after maturity.

(ii) According to Section 11 of the Indian Contract Act, 1872, a person who is of the age of majority is competent to enter into any contract. The Majority Act of 1875 states that every person domiciled in India shall attain the age of majority on completion of 18 years and not before. Therefore, a person who has completed the age of 18 years is a major and otherwise he will be treated as minor.

In the instant case, Ramesh who is a minor is not competent to enter into a contract and any agreement with him is void [Mohiri Bibi v Dharmodas Ghose 1903, 30 Cal, 539 (PC)]. Section 68 of the Indian Contract Act, 1872 however, prescribes the liability of a minor for the supply of the things which are the necessaries of life to him. It says that though minor is not personally liable to pay the price of necessaries supplied to him or money lent for the purpose, the supplier or lender will be entitled to claim the money/price of goods or services which are necessaries suited to his condition of life provided that the minor has a property. The liability of minor is only to the extent of the minor's property. This type of contract is called a Quasi-contract and the right of the supplier/lender is based on the principle of equity.

Therefore, in view of the position explained above, Suresh will be entitled to recover the amount of loan given to Ramesh for payment of the college fees from the property of the minor.

(iii) In accordance with the provisions of the Payment of Gratuity Act, 1972, as contained in Section 4(1), Gratuity shall be payable to an employee on the termination of his employment after he has rendered continuous service for not less than 5 years, on his superannuation, or on his retirement or resignation, or on his death or disablement due to accident or disease. The condition of the completion of 5 years continuous service is not essential in case of the termination of employment of any employee due to death or disablement. Disablement means such disablement as incapacitates an employee for the work which he was capable of performing before the accident or disease resulting in such disablement.

In the light of the above, the condition of the completion of 5 years continuous service is not essential and therefore, the contention of company is not valid. X, is therefore, entitled to claim gratuity in the given case.

Question 2(c)

(i) State with reasons whether the following persons are entitled to receive bonus under the Payment of Bonus Act, 1965:

- A. An apprentice under the Apprentice Act.**
- B. A probationer**
- C. An employee employed through contractors on building operations**
- D. A retrenched employee**
- E. A dismissed employee reinstated with back wages**

(ii) When an employee becomes disabled due to any accident or disease and is unable to do the same work and re-employed on the reduced wages, how the gratuity of such employee

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

shall be computed under the provisions of the payment of Gratuity Act, 1972?

(iii) X agreed to become an assistant for 5 years to Y who was a doctor practicing at Chennai. It was also agreed that during the term of agreement X will not practice on his own account in Chennai. At the end of one year, X left the assistantship of Y and began to practice on his own account. Referring to the provisions of the Indian Contract Act, 1872, decide whether X could be restrained from doing so?

[5+4+3=12]

Answer:

(i) Entitlement to Bonus:

- A. **Apprentice:** An Apprentice who is an apprentice under the Apprentice Act is not entitled to bonus, as apprentice is specifically excluded from 'Employee' under section 2(13).
- B. **Probationer:** A probationer is an employee and as such is entitled to bonus provided he has worked in the establishment for not less than 30 working days in the accounting year (section 8) Confirmation of the employee is not a necessary requirement.
- C. **An employee employed through contractors on building operations** is entitled to bonus as section 32(vi) has been deleted by Payment of Bonus (Amendment) Ordinance, 2007.
- D. **Retrenched Employee:** He is eligible to get bonus provided he has worked for minimum qualifying period. {East Asiatic Co. (P) Ltd. v Industrial Tribunal}
- E. Employee includes a person who is no longer in service (Explanation under Section 21). A **dismissed employee reinstated with back wages** is entitled to bonus. (Commom India Ltd v Neeranjan Das)

(ii) Computation of Gratuity of a disabled employee: According to Section 4(4) of the Payment of Gratuity Act, 1972, when an employee becomes disabled due to any accident or disease and is not in a position to do the same work and re-employed on reduced wages on some other job, the gratuity will be calculated in two parts:-

- (1) For the period preceding the disablement: on the basis of wages last drawn by the employee at the time of his disablement.
- (2) For the period subsequent to the disablement: on the basis of the reduced wages as drawn by him at the time of the termination of services.

In the case of Bharat Commerce and Industries Vs. Ram Prasad, it was decided that if for the purposes of computation of quantum of the amount of gratuity the terms of agreement or settlement are better than the Act, the employee is entitled for that benefit but the maximum statutory ceiling limit as provided under Sub-section (3) of Section 4 of the Act cannot be reduced by mutual settlement or agreement.

(iii) According to Section 27 of the Indian Contract Act, 1872, in any agreement through which a person is restrained from exercising a lawful profession or trade/business/ is void.

However, an agreement of service by which a person binds himself during the term of the agreement not to take service with anyone else directly or indirectly to promote any business in direct competition with that of his employer is not in restraint of trade. In such a situation the agreement is valid.

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

In the instant case, X has agreed not to practice on his own account during the term (5 years) of agreement. After one year, X left Y and began to practice on his own account. Therefore, as per the above provisions, X can be restrained by an injunction from practicing on his own account in Chennai.

Question 2(d)

(i) Mr. D started "Self Service" system in his shop. Mr. A entered the shop, took a basket and after taking article of his choice into the basket reached the cashier for payments. The cashier refused to accept the price. Can Mr. D be compelled by Mr. A to sell the said article? Decide.

(ii) State the rights and liabilities of 'A' in the following cases;

- A. 'A' is owner of the factory building and also product. 'A' authorizes 'B' to take an insurance policy on factory building for ₹2 lacs.'B' procures a policy for ₹2 lacs on factory and another policy for ₹2,000 on products. 'A' refused to reimburse to 'B'**
- B. 'A' authorizes 'B' to buy 500 pieces of sunlight soap for him but 'B' buys 500 pieces Henko at a price of ₹5,000. 'A' refused to pay to 'B'**
- C. An Auctioneer advertised in a newspaper that sale of office furniture will be held at Kolkata on 29.10.2014. 'A' came from New Delhi to buy the furniture but the auction was cancelled. Whether 'A' can file a suit against the auctioneer for his loss of time and cost.**

(iii) Mr. A agreed to purchase 100 bales of cotton from 'B' from his large stock. 'A' sent his men to take delivery of cotton. On completion of packing of only 70 bales there was accidental fire and entire stock including packed 70 bales were destroyed. There was no insurance cover. Who will bear the loss?

[4+6+2=12]

Answer:

(i) An invitation to offer is an act precedent to making an offer. It is done with intent to generally to induce and negotiate. An invitation to offer gives rise to an offer after due negotiation and it cannot be per se accepted. In an invitation to offer there is no expression of willingness by the offeror to be bound by his offer. It is only a proposal of certain terms on which he is willing to negotiate. It is not capable of being accepted as it is.

In *Harvey v Facey* [1893] AC 552 Privy Council succinctly explained the distinction between an offer and an invitation to offer.

In the instant case Mr. A entered the shop, took a basket and after taking article of his choice into the basket reached the cashier for payments. The cashier refused to accept the price. The display of articles with a price in a self-service shop is merely an invitation to offer. It is not an offer for sale. Therefore, Mr. A cannot compel the cashier Mr. D to sell the-said article. [*Fisher v Be*/(1961)]

(ii)

- A.** In this case "B" was authorized to pay premium for a policy for the factory building at ₹2 lacs. "B" was not authorized to take a policy for the products. Hence 'A' is bound to pay for the insurance of the factory building.

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

- B.** In this case, the agent i.e. "B" does more than he is authorized to do and the amount of ₹5,000 cannot be separated between sunlight and Henko. "A" may repudiate the whole transaction. As per contract principal is not bound when excess of Agent's Authority is not separable.
- C.** 'A' cannot file a suit against the Auctioneer for his loss of time and cost because the Advertisement was merely a declaration of intention to hold Auction.

(iii) Since 70 bales were ascertained and appropriated, property in those 70 bales was transferred to A, hence A is liable for 70 bales only and B is liable for remaining stock.

Question 2(e)

(i) State the exceptions to the consequences of not registering a partnership firm.

(ii) Comment on the following :

- A.** Daily working hours in a factory cannot be more than 8 hours on any day considering ceiling of 48 working hours in a week as per the Factories Act 1948.
- B.** An individual dispute is not an industrial dispute under the Industrial Disputes Act, 1947.
- C.** W, a heart patient worked for four hours in a factory premises. He profusely sweated during the recess and died of heart failure which resulted on account of severe stress and strain inside the factory premises. Is the employer liable to pay compensation under the Employees Compensation Act, 1923?

(iii) Arun entered into a contract with Barun to let out the house under construction and received advance of ₹ 2 lakhs. The house was, however, requisitioned by government and, therefore, Arun failed to honour the contract. Can Barun recover damages for breach of contract? Justify.

[3+6+3 = 12]

Answer:

(i) Non-registration would not affect the following - [Sec. 69]

1. Right of third parties to sue the Firm or any Partner.
2. Right of Partners to sue for - (a) Dissolution of the Firm, or (b) Settlement of accounts of a dissolved Firm, or (c) Realising the property of a dissolved Firm.
3. Power of an Official Assignee, Receiver or Court to realise the property of an Insolvent Partner and to bring an action on behalf of the Insolvent Partner.
4. Rights of the Firm or the Partners of the Firm which has (a) no place of business in the territories to which the Act applies, or (b) whose places of business are in such territories to which the Chapter does not apply.
5. Right of the Firm to institute a suit or claim of set-off not exceeding ₹100.
6. Right of an Unregistered Firm to bring a suit against third parties to enforce a right arising otherwise than out of a contract, e.g., for enforcing a trademark.

(ii)

- A.** As per Sec . 51 of the Factories Act, 1948 no adult employee is required to work more than 48 hours in any week. Subject to this rule, no adult employee shall be required to work for more than 9 hours in any day. But in order to facilitate the change of shift, this limit may exceed. This can, however, be done with the previous approval of the Chief Inspector of Factories.

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

- B.** Where any employer discharges, dismisses, retrenches or otherwise terminates the services of an individual workman, any dispute or difference between that workman and his employer connected with, or arising out of, such discharge, dismissal, retrenchment or termination shall be deemed to be an industrial dispute notwithstanding that no other workman nor any union of workmen is a party to the dispute. [Sec 2-1]
- C.** According to Section 3 of the Employees Compensation Act, 1923, employer is liable to pay compensation if personal injury is caused in course of employment. The course of employment is not interrupted by intervals of rest. So the employer is liable to pay compensation in the given case.

(iii) No, Barun is not entitled to recover damages for breach of contract from Arun because there is unforeseen change in the law due to requisition of the property by the Government. At best Barun can recover his advance provided there is a covenant to the agreement in this respect.

If a contract contains an undertaking to perform impossibility, it is void ab initio. This rule is based on the maxim that, what is impossible does not create an obligation. A situation of impossibility may have existed at the time of entering into the contract or it may have transpired subsequently (also known as supervening impossibility). In the instant case, the impossibility arises due to requisition of land by the Government.

Question 3: Answer any 2 questions

Question 3(a)

- (i) Can a listed company change its name as and when necessary? Give reasons to support your answer.**
- (ii) Priya Ltd. Co. issued and published its prospectus to invite the investors to purchase its shares. The said prospectus contained false statements. Mr. Lal purchased some partly paid shares of the company in good faith on the stock exchange. Subsequently, the company was wound up and the name of Mr. Lal was in the list of contributors. As per the provisions of Companies Act, 2013, Analyse:**
- A. Whether Mr. Lal is liable to pay the unpaid amount?**
- B. Can Mr. Lal sue the directors of the company to recover damages?**

[3 + 5 = 8]

Answer:

(i) As per section 21 of the Companies Act, 1956 a company may, by special resolution and with the approval of the Central Government signified in writing, change its name, provided that no such approval shall be required where the only change in the name of a company is the addition thereto or, as the case may be, the deletion there from, of the word "Private", consequent on the conversion in accordance with the provisions of this Act of a public company into a private company or of a private company into a public company.

(ii) Firstly, Mr. Lal is not the original allottee of shares, since he purchased shares from the secondary market, viz. stock exchange.

- A.** Mr. Lal is liable to pay the unpaid calls, since he holds partly paid shares and he is liable as a contributory

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

- B. Mr. Lal cannot sue the directors to recover damages, since Mr. Lal has no cause of action against the company or the directors as he did not subscribe for the shares on the faith of a misleading prospectus. Mr. Lal had procured the shares from the stock exchange.

Question 3(b)

(i) "Right to Information Act, 2005 primarily envisages setting out a practical regime of right to information for citizens to secure access to information under the control of public authorities". Hence it should provide access to all information. Justify.

(ii) Who is a PIO and what is his duty?

[6 + 2 = 8]

Answer:

(i) It is true that "Right to Information Act, 2005 primarily envisages setting out a practical regime of right to information for citizens to secure access to information under the control of public authorities". But all information need not be disclosed. The following are exempt from disclosure:

1. Information affecting national security, economic interest and relation with foreign State.
2. Information forbidden to be published by any court.
3. Information privileged to parliament or the State Legislature.
4. Information including commercial confidence, trade secrets or intellectual property, the disclosure of which would harm the competitive position of a third party.
5. Information available to a person in his fiduciary relationship.
6. Confidential information received from a foreign Government.
7. Information endangering the life or safety of person.
8. Information affecting any investigation or prosecution proceedings.
9. Cabinet papers.
10. Information invading the privacy of an individual.
11. Information disclosure of which would involve an infringement of copyright.
12. Information pertaining to specified intelligence and security organization established by central Government and notified organizations by a State Government.

(ii) Every public authority shall designate as many public Information Officers (PIO) and Assistant Public Information Officers (APIOs) as may be required for each of its administrative units or officers.

A PIO shall deal with requests from persons seeking information and render all reasonable assistance to them. He shall dispose of the request as expeditiously as possible, but within maximum 30 days, either by providing the information or rejecting the request.

Question 3(c)

(i) Highlight the role of institutional investors in promoting good Corporate Governance.

(ii) Write a short note on 'Related Party Transactions', with reference to accounting standards.

[5 + 3 = 8]

Answer:

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

(i) Institutional investors can have a lot of influence in the management of corporations because they are entitled to exercise the voting rights in a company. They can engage in active role in corporate governance. Furthermore, because institutional investors have the freedom to buy and sell shares, they can play a large part in which companies stay solvent, and which go under. Influencing the conduct of listed companies, and providing them with capital are all part of the job of investment management.

Expectation of their role and recommendations:

Institutional shareholders should reflect the following characteristics:

1. Take active interest in the composition of board of directors.
2. Be vigilant
3. Maintain regular and systematic contact at senior level for exchange of views on management, strategy, performance and quality of management.
4. Ensure that voting intentions are translated into practice
5. Evaluate Corporate Governance performance of the company

Internationally, special codes have been issued to give guidance to institutional investors on how they can positively influence corporate governance for e.g. UK Stewardship Code.

Institutional investors will have a lot of influence in the management of corporations because they will be entitled to exercise the voting rights in a company. They can engage in active role in corporate governance. Furthermore, because institutional investors have the freedom to buy and sell shares, they can play a large part in which companies stay solvent, and which go under. Influencing the conduct of listed companies, and providing them with capital are all part of the job of investment management.

(ii) 'Related-Party Transaction' is a business deal or arrangement between two parties who are joined by a special relationship prior to the deal. It may be defined as a transfer of resources or obligations between related parties, regardless of whether or not a price is charged.

Accounting Standards (AS 18) defines the terms related party and related party transaction. Related party is defined as parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

The Board is duty bound to have control over Related party and Related Party Transactions. It is the responsibility of the Board to ensure that such transactions are just, fair and total in the interests of the company.

Question 4: Answer any 2 questions

2 X 8 = 16

Question 4(a)

(i) **“Ethics is the first line of defense against corruption, while law enforcement is remedial and reactive. However, both fail to achieve the desired aim in the Indian set-up. “Do you agree? Give reasons in support of your answer.**

(ii) **Write notes on Social and ethical accounting.**

[5+3=8]

Answer:

(i)

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

- A. It is absolutely correct to say that ethics is the first line of defense against corruption. What prevents corruption in the first is ethics. The enforcement of law is a reaction to the occurrence of the corruption. While the law can only lay down the do's and don'ts and the consequences of doing or not doing something, the compliance to law in letter & spirit can be achieved only through ethical practices being followed.
- B. An act may be perfectly legal but totally unethical. Therefore, the statement law enforcement is remedial and reactive is also true.
- C. However, ethics is not absolute and is open to the influence of time, place and situation. Certain unethical practices on account of the fact that it is widely prevalent are apparently justified.
- D. The following are some of the factors that have contributed to the prevalence of corruption in India:
- (a) Cultural ethos: Putting a premium on materialization, profiteering, power-play and casual attitude for ethical values. Myopic concerns over-riding long-term considerations and values.
 - (b) Institutional failures: Procedural rigmaroles, in-built obstacles, bureaucratic redtapism etc.
 - (c) Poor enforcement of law: delays in justice.
- Erosion of values in politicians, entrepreneurs; political lobbying etc.

(ii) Social and ethical accounting:

It is a process that helps a company to address issues of accountability to stakeholders, and to improve performances of all aspects i.e., social, environmental and economic. The process normally links a company's values to the development of policies and performance targets and to the assessment and communication of performance.

Social and ethical accounting has to standardized model. There is no standardized balance sheet or unit of currency. The issues are defined by the company's values and by the interests and expectations of its stakeholders, and societal norms and regulations. With the focus on the concerns of society and ethical accounting framework implicitly concerns itself with issues such as economic performance, working conditions, environmental and animal protection, human rights, fair trade and ethical trade, human resource management and community development, and hence with the sustainability of a company's activities.

Question 4(b)

(i) "A Commitment by corporate management to follow an ethical code of conduct confers a variety of benefits". What are these benefits?

(ii) Discuss briefly "Ethics in compliance".

[5+3=8]

Answer:

(i) More and more companies recognize the link between business ethics and financial performance. Companies displaying a "clear commitment to ethical conduct" consistently outperform companies that do not display ethical Code of Conduct is formal statement that describe what an organization expects of its employees.

Adherence to a code of Conduct offers some advantages. It deters wrongdoing and promotes:

- A. Honest and ethical conduct including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships.

Answer to PTP_Intermediate_Syllabus 2012_Dec 2014_Set 1

- B. Full, fair, accurate, timely, and understandable disclosure in reports and documents that a company files with, or submits to the Commission and in other public communications made by the company.
- C. Compliance with applicable governable laws, rules and regulations.
- D. The prompt internal reporting of violations of the code to an appropriate person or persons identifies in the code, and
- E. Accountability for adherence to the code.

(ii) Compliance is about obeying and adhering to rules and authority. The motivation for being compliant could be to do the right thing out of the fear of being caught rather than a desire to be abiding by the law. An ethical climate in an organization ensures that compliance with law is fuelled by a desire to abide by laws. Organizations that value high ethics comply with the laws not only in letter but go beyond what is stipulated or expected of them.

Question 4(c)

“It is now well recognized that the business ethics and financial performance of companies are interlinked”. Discuss this statement. [8]

Answer:

Business 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 organizations. Ethical behavior and corporate social responsibility can bring significant benefits to a business. Companies displaying a “clear commitment to ethical conduct” consistently outperform companies that do not display ethical conduct.

(1) Attracting and retaining talent:

People aspire to join organizations that have high ethical values. Companies are able to attract the best talent and an ethical company that is dedicated to taking care of the organization. The ethical climate matter to the employees. Ethical organizations create an environment that is trustworthy, making employees willing to rely, take decisions and act on the decisions and actions of the co-employees. In such a work environment, employees can expect to be treated with respect and consideration for their colleagues and superiors. It cultivates strong teamwork and productivity and support employees' growth.

Retaining talented people is as big a challenge as getting them in the first place.

Work is a means to an end for them, the relationship they have with their employer must be mutual, win-win one, in which their loyalty should not be taken for granted. Talented people will invest their energy and talent only in organizations with values and beliefs that match their own. In order to achieve this match, managers need to build cultures, compensation and benefits packages, and career paths that reflect and foster certain shared values and beliefs.

(2) Investor Loyalty:

Investors are concerned about ethics, social responsibility and reputation of the company in which they invest. Investors are becoming more and more aware that an ethical climate provides a foundation for efficiency, productivity and profits. Relationship with any stakeholder, including investors, based on dependability, trust and commitment results in sustained loyalty.

(3) Customer Satisfaction:

Customer satisfaction is a vital factor in successful business strategy. Repeat purchases orders and enduring relationship of mutual respect is essential for the success of the company. The name of a company should evoke trust and respect among customers for enduring success. This is achieved by a company that adopts ethical practices. When a company because of its belief in high ethics is perceived as such, any crisis or mishaps along the way is tolerated by their ethics to survive a critical situation. Preferred values are indentified ensuring that organizational behaviours are aligned with those values. An organization with a strong ethical environment places its customers' interests as foremost. Ethical conduct towards customers builds a strong competitive position. It promotes a strong public image.

(4) Regulators:

Regulators eye companies functioning ethically as responsible citizens. The regulator need not laws monitor the functioning of the ethically sound company. The company earns profits and reputational gains if it acts within the confines of business ethics.