Strategic Management – The Competitive Edge
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Lecture 10
Responsibilities of Business

In the last session we looked at the 4 Responsibilities of Business. One is the economic the firm has to do economic activity in order to be in the market place that is it must do . This economic activity which the firm does has to conform to legal accepted boundaries, that is legal. The third is ethical that is the firm has to follow certain ethical principles with respect to its business.

So, making false claims about the product which it puts out into the market are not ethical business; the firm should desist from doing all this. The last one is discretionary. What is discretionary? Discretionary is which the firm might consider doing if everything is okay with respect to the firm. There are some discretionary activities which the firm can consider doing- this we call Corporate Social Responsibility. Chapter3 of my Book on Strategic Management gives you corporate governance.

Many real market happenings are listed here. The one which you can read with interest is the case of the Eastman Kodak Company. So, period 1983 to 1993 saw the company falling from the top 10 to bottom 18 of the most admired companies. So, the person who was responsible to bring the Eastman company back on wheels was the new CEO George Fisher. What did he do? He said cost cutting alone would not be the answer, company should look for growth opportunities in imaging as well as start divesting non-core businesses.

So, this was the type of suggestion made and this worked for the company. Kodak represents a classic case of how the company had failed to adjust to the changing environment by its lack of strategic response. So, in other words, what we were discussing in the earlier sessions, the role of the CEO becomes very important. He is the real motivator, the person who can be the harbinger of the fortunes of the firm. So many firms have really found that their fortunes have changed. Many cases to the better; some cases nosedived because of the CEO vision.

Chapter number 4 of the book looks at the code and laws for Corporate Governance. It discusses basically 4 committee reports. One is the Cadbury committee report, second one is the CII committee report,third one is the Kumara Mangalam Birla report, and the fourth one is the Narayan Murthy committee report.

Cadbury committee report: it was set up in May 91 by the financial reporting Council of the

London Stock Exchange. The major recommendations are given on page number 54 of my Strategic Management Book. CII report is our own Confederation of Indian Industry report in 1996 and the Kumar Mangalam Birla committee report in 1999, set up by SEBI the Securities and Exchange Board of India. The major recommendations are given on page numbers 55 and 56 of the Book. The next one is the Narayan Murthy report, this was in 2003.Some of the recommendations of the report are listed on page number 56

What are the main recommendations? All audit committee members should be financially literate- kindly note this term financially literate, and at least one member should have accounting or related financial management expertise. This is very important because so, many financial bunglings are reported in the present-day setup.

So, the board of directors will be better served if they have these types of members; they can know what is really happening, mere explanation as to why a company has followed a different accounting standard from the prescribed standards will not be sufficient. Example, suppose you are operating only in India there is no need for you to follow the US standards- that is optional. Suppose you are catering to both the markets-you can follow US standards and the Indian standards.

Board members should be informed about risk assessment and minimization procedures. This is very important, because board will not be able to go through minutely many of the matters which are put up to the board for consideration of investment.

Infosys has a person at the level of Vice President for risk assessment. So, any investment, which the company makes, the Vice President has to give his inputs to the board- is it worth going about? What are the different scenarios? What are the different alternative scenarios; board members should be trained in the business model of the company as well as the risk profile of the business parameters.

So, in other words, a board member should not be a dummy person, he comes to the board meeting and walks off. Their responsibilities as directors and best ways to discharge them- he should be conversant, use of proceeds of IP which should be disclosed to the audit committee. I was referring to this as so many bunglings in the present day committees set up by companies. So, similarly, with respect to IPOs, you receive money. How is this being used- all this should be disclosed to the audit committee.

There should be no or few nominee directors; when a director is to be appointed on the board, shareholders shall make such appointments. Board of Directors limits the maximum number of stock options that can be granted to non-executive directors in any financial year; may fix compensation paid to non-executive directors. Whistle blowers should not be subjected to unfair or prejudicial employment practices.

A peer group comprising the entire board of directors, excluding the director being evaluated, should make the responsibilities and the performance evaluation of non- executive board members.

There was one more committee that is the Naresh Chandra committee in 2002; it also did work on the corporate governance issues.

It was given the task of analysing and recommending changes if necessary, in various areas like statutory auditor company relationship, independence of auditing functions, certification of accountants and financial statements by managers and directors adequacy of regulation of Chartered Accountants, company secretaries, cost accountants and other similar statutory oversight functionaries, the role of independent directors, etc.

In 2013 the Companies Act was amended by the parliament. The salient features of this amendment is listed on page number 58. Suppose some of you are interested to go through in more detail on these issues- refer to the Gazette of India extraordinary part 2, section 1 number 27 August 30 2013.

So, with all this, the responsibility of doing business becomes even more categorical. All these heads economic, legal, ethical and discretionary- they are under different boundaries. So, a company cannot violate these boundaries; if it violates, it will be subject to stringent actions.

So, this is what is happening in the present day set up in the Indian context. So, if you really look at what is happening to many of the Chinese firms, the government came down with a heavy hand- so many financial bunglings happened, non-existent directors were shown. So, these are all unethical practices, which were done by the companies and it was detected and the government took prompt corrective actions to see that these things do not recur.

So, this is what is happening in the present today globalized scenario in the Indian context. So, India wants to become a 5 trillion dollar economy and in order to achieve that, many steps are being taken, including the Make in India and to become self-sufficient in so many sectors.

Now, with all this we go further on social responsibility; the social responsibilities, as I mentioned, coming under the head of ethical and discretionary; ethical responsibility looks at utility. What is this utility? Does it optimize the satisfaction of the stakeholders; should behave in such a way that it produces the greatest benefit to the society and least harm, at the lowest cost.

Then rights, what are rights? Does it respect the rights of the individuals involved? The third one on justice -is it consistent with the canons of justice? Decision makers should be equitable, fair and impartial in the distribution of costs and benefits to individuals and society. In other words, you are really to act as a person following the norms of justice, not be biased.

So, these are the heads of this ethical responsibility. And the first firm, incidentally, to do this social audit in the country was a public sector firm. Again, kindly note that the role of the public sector has been very considerable. Right from corporate planning down to social responsibility. They have taken lots of initiatives.

The company that I am referring to is IPCL- Indian Petrochemicals Limited and the period was December 1987. So, the social audit came into India in 1987 only. So, even to this day, the social audit system is not really there in many of the so called developed countries, but when we look at India, we are much ahead.

IPCL with respect to social audit in 1987, formed 4 groups one was employees, second was customers, third was government, fourth was social;it gave a weightage to each of these groups, the weightage given was equal weight- that is 25 percent to each group after giving this weightage these were called focus groups for social audit. So, when you do social audit, you should necessarily have focus groups.

Now, when they got the inputs from the employees, the factors and the sub factors highlighted by the employees were hygiene; then majority satisfactory or not satisfactory. So, when you are looking at satisfaction, you are looking at organizational policies, working conditions, growth, job satisfaction, employee employer relationship, hygiene is the ambience of the workplace. Obviously, you are looking at neat workplaces, including toilets etc. So, everything should be kept clean.

The second is what is expected from the customer side, the customer wants the company to do product development, not be stagnant. So, nothing like frog in a well type of policy, I do the same product for years on end; no, especially in the present market situation, if you do not concentrate on new product development, you may have to close shop before you could even think that this coming because the competitor will come out with something new. Then the product attributes, service attributes and promotion. So, for the sub factors also weightage was given for product development 30 percent, for product attributes 30 percent, service attributes 20 percent and promotion 20 percent.

Then with respect to government, what is it that the government may be interested in with respect to public sector, one is whether it has paid its tax on time regularly and the dividends, adherence to rules and regulations. Then other conditions to economy. Each of these sub factors are again given weightage. So, the tax portion given 30, then rules and regulation given 20 other conditions to economy given 50.

Then the last aspect with respect to society, what are the sub factors? So, what is the first quarter community welfare- Rural Development charities and relief measures, each of them having separate weightages.

Now, when you looked at the report these scores with respect to each of these groups giving an indication of IPCLs corporate responsibility. It came out to be 6.125 out of 10 employees got score of 5.1, customers 5.8, government 7, society 6.6. So, the overall score came to 6.125 out of 10. This was the first initiative taken by a public sector company back in 1987.

Now, if you look at the present today scenario many of the companies whether it is public sector or private sector they are into this field of CSR. So, you take the examples of Infosys or the Tata Group companies- they have made significant contributions to the field of CSR.

So, if you go to page number 64 of chapter 5 in my book on strategic management, it gives you CSR activities mandated by the government of India; now this is also incorporated in the 2013 companies act. These guidelines are applicable to every company having a net worth of 500 crores or more or a turnover of 1000 crores or more or a net profit of 5 crores or more.

Now, what does it entail? It entitles forming a CSR committee, the committee would comprise of 3 or more directors at least one of who should be an independent director. The composition of the committee needs to be included in the board's report. So, when you are making a board presentation, whether it is a quarterly or annual, especially with reference to software companies, all these things have to come out.

The committee would formulate the policy including activities specified in scheduled 7; schedule 7 forms an important schedule under the Companies Act, some of them are listed here: eradicating extreme hunger and poverty, promotion of education, promoting gender equality and empowering women, reducing child mortality and improving maternal health,combating Immunodeficiency virus, acquired immune deficiency syndrome, malaria and other diseases ensuring environmental sustainability, employment of enhancing vocational skills, social business projects, contribution to Prime Minister's national relief fund - all these coming under the CSR activities.

So, one of these initiatives which was taken up by 2 individuals, who are the promoters of

Mindtree in Indian Institute of Science itself is with reference to the medical field by 2 founders of Mindtree, Parthasarathy and Subroto Bagchi. IISc is likely to come up with a sophisticated multi-speciality hospital soon to cater to many of the things which are mentioned in this schedule 7. So, these are so many of the CSR initiatives taken in the present today Indian context. We stop here. We will continue in the next session. Thank you.