Department of Business Administration

B U S I N E S S   E T H I C S

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Name of the Teacher **:** Sneha Dutta

Name of the Topic **:** *Role of auditors in Corporate Governance : Governance & Internal auditor ;Whistle Blowing – Kinds of Whistle Blowing , precluding the need for Whistle Blowing.*

Role of auditors in Corporate Governance

Corporate governance refers to the way a company directs and controls its institutional systems, ethics and accounts. It focuses on promoting transparency and fairness within establishments and organizations by monitoring performance and ensuring accountability.

As per the Organization for Economic corporation and development (OECD) documents (1999), Corporate Governance (CG) is the system by which organization are directed and controlled. Corporate governance designed to keep intact and disclose to shareholders in manner truly reflect the position of corporate.

Milton friedman (1962) suggested that corporate governance is to carry out the business in accordance with owners (promoters) and shareholder's aspiration, which generally will be to make as such money as possible, while in compliance to the fundamental rules of the society embodied in law and local customs. He talked about shareholders capitalism. Corporate governance means doing the whole thing superior, to get better relation between companies and their shareholders, full disclosure of information to all stakeholders and to monitor executive management properly in the interest of shareholders.

Cadbury Committee Report (1992) defines Corporate Governance as "the system by which companies are intended for and restricted". It is generally understood as the framework of rules, regulations, relationships, system and processes within and by which authority is exercised and controlled in corporations.

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Kumar Mangalam Birla Committee Report (1999) mentioned that corporate governance is essential intention to enhance long – term shareholders value and to protect interest of other stakeholders.

Aravanan (2001) suggested that CG is basically system of making directors accountable to the stakeholders for effective management of the companies, with concerns of ethics and value. This is related to Board of directors who are members of auditing committee too, whose role is to check transparency, integrity and accountability of the management toward shareholders and investing community.

Shareholder's value is enhanced by honest and transparent board of Directors. (Vepa Kamesam, 2006). Jyothi Dhawan identifies the role of board of directors in CG, which inculcate a sense of accountability towards all stakeholders. The audit committee would search for the integrity and reliability of financial statement and reassure shareholders. (AICPA, 1967; Auerbach, 1973 and FCCG, 1999).

The responsibility of audit committee in the area of corporate governance is to provide assurance that the corporation is in rational compliance with relevant laws and regulations, is conducting its affairs fairly, and is maintaining effective controls against employee conflict of interest and fraud.(Muhammad Faisal Siddiqui) An audit committee consisting independent directors can have control over management and thereby acting as a sort of assurance to the shareholders that they will have full disclosure of correct information. To have good corporate governance, audit committee needs resource persons to act as independent director on whose shoulder lies the responsibility to take the company in the right path, demand for more disclosures, transparency and accountability and performance standards for investors and lender and protection for shareholders. (Abhas)

The shareholders of the company place very high trust on the auditor's report, which apparently shows the true and fair view of the accounts of the company. The auditor should perform their duties with extreme care and vigilance to ensure that there is no illegal or improper transaction. (Harsh Gargani and Ritika Jhurani, 2009). Auditor independence would be safeguarded if audit committee were made up of a majority of independent and non – executive directors, and this might signify that their independent status would contribute to auditor's independence through bridging communication network. (Zulkarnain Bin Muhamad Sori, Shamsher Mohamad and Mohd Saad. (2008). Knapp (1987) found that an audit committee if is more likely to support the auditor rather than the management in audit differences and the level of support is steady across members of the audit committee which will secure interest of shareholders too. Department of Company affairs guidelines (2000) have recommended proper disclosure to the shareholders and investing community, which is done by role and influence of auditing committee only. The problem in Indian Corporate Sector is that of controlling the leading shareholders and safe guarding interest of minor shareholders, which can be

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solved by board of directors who are accountable to all stakeholders; it would make governance more easy (Jayant Rama Varma, 1997).

In that regard, internal & external auditors serve as one of the primary protectors of corporate governance in any organization.

1.Represent Interest of Shareholders

One of the primary roles of external auditors in corporate governance is protecting the interests of shareholders. This is possible because external audition reports are conducted independent of the company's influence. External auditors report the state of a company's finance and attest to the validity of financial reports that may have been released. They ensure that the board receives accurate and reliable information. The board may also question the auditors' views and assessment on the appropriateness of the accounting principles used by a company.

2.Promote Accountability

External auditors may introduce measures and policies designed to compel accountability in the workplace. For instance, auditors could recommend penalties for officers who manipulate financial statements by inflating figures or cooking accounting numbers. Penalties for such acts could include stripping the manager of his position or his compensation, such as reducing annual bonuses, and even pensions.

3.Risk Assessment and Mitigation Planning

External auditors help promote corporate governance by conducting period risk assessment. Auditors review the security measures that a company has in place against corporate fraud or corruption. In addition to assessing potential risks, auditors also analyze the overall risk tolerance of the company as well as the efforts the company has made toward mitigating risks. For instance, if a company or government agency has an under-performing whistleblower system, efforts may be made to improve this.

4.Crisis Management

External auditors can help ensure good corporate governance by developing efficient crisis-management plans to be used in the event of allegations of fraud or corruption. The plan typically involves assigning responsibilities to different administrative officials. This way, if the company becomes involved in a financial crisis, officials have an active plan that they can use in sustaining confidence among investors. Crisis-management plans may also include control measures that are to be used with the media and law-enforcement officials.

5.Maintain Strong Relationship with Regulators

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The efforts of an external auditor help foster a good relationship with regulators. Most regulators are supportive of companies and agencies that appear to have transparent operations. External auditors evaluate the organization of a company for compliance with regulations. Regulators are also more likely to trust company disclosures after an auditor attests to them.

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Introduction to the concept of Whistle Blowing

Whistle blowing refers to the act of organisation members, either former or current, disclosing information on illegal and unethical practices within the organisation to parties internal or external to the organisation, who can take action. It is becoming increasingly common as more and more employees speak out about their ethical concerns. It cannot be denied that whistleblowing is accompanied by a range of problems, for both the whistleblower and the organisation. However, it can be argued that whistleblowing is an important and valid method of endeavoring to control possible unethical behaviour by organisations, as well as helping to establish a level of social responsibility. For these reasons, it is important for society to maintain a level of support and encouragement towards whistleblowers, so that their often valuable contribution towards eliminating corporate wrongdoings can continue.

Employees who discover apparent wrongdoing within an organisation are faced with several options, each of which comprise of both negative and positive aspects. Generally, a whistleblower may hesitate to report wrongdoings either internally or externally due to a fear of losing their job or being transferred to an undesirable location, being subjected to harassment and victimisation (Lewis, 1997), having their lifestyle, competence and mental health questioned, and becoming a focus of public attention, resulting in a loss of privacy (Criminal Justice Commission [CJC] 1999, p. 2). As well, they may struggle with a sense of disloyalty, where they inadvertently feel as if they are betraying their fellow colleagues or organisation if they report what they know. Larmer (1992 cited Jones 1996) states that a loyal employee will discern that any unethical behaviour can never be in the best interests of an organisation, and to ignore it with silence is in itself disloyal. Conversely, the final dilemma a whistleblower may face is one of personal loyalty, to their own ethical and moral values. Nevertheless, obligations of confidentiality and loyalty ideally should not take precedence over the fundamental duty to act in a manner that prevents unnecessary harm to others.

While these are all valid concerns, it is important for a whistleblower to concentrate on the positive aspects that reporting the wrongdoing can have. The CJC (1999, p. 32) states in its report that "over time,

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whistleblowing will increasingly be regarded as a normal workplace responsibility". When a whistleblower exposes the corrupt deeds of an organisation, they are not only acting ethically and responsibly, they are also serving to encourage those same qualities throughout the community. Other obvious benefits resulting from blowing the whistle include putting an end to the wrongdoing and those being disadvantaged by the wrongdoing, bringing to justice the individuals or organisation accountable for the wrongdoing, avoiding potential damage to the health and safety of the community, stopping potential damage to the environment, and creating an opportunity to implement improved internal practices in order to prevent wrongdoing in the future (CJC 1999, p. 2).

Any potential whistleblower must realise that a well thought-out approach is both essential and practical. Firstly, be positive the situation is one that warrants whistle blowing. Secondly, carefully examine the motives behind the whistleblowing in order to ensure that they are genuine and can serve the public interest. Next, verify and document all information, as this will help to add further credence and strength to disclosures (CJC 1999, p. 13). Fourth, determine to whom the wrongdoing should be reported, and if the internal or external route is best. The allegations should then be stated in a clear, concise and objective manner. Lastly, ensure that all appropriate guidelines have been followed in reporting the wrongdoing. Coyne (2003) recommends consulting a well-informed lawyer in order to help a whistleblower determine the best course of action to take, as well as what protection is available to the whistleblower. The CJC (1999, p. 36) recommends that in order to sufficiently prepare themselves, potential whistleblowers need to understand that they may be unfairly vilified.

There are many occurrences where whistleblowing has deflected considerable harm towards society. One such example illustrated by Jennings (2003), is that of Jerome J. LiCari, a former director of research and development for Beech-Nut Nutrition Corporation. Due to the low cost of the apple product used in most of the organisation's fruit foods, Mr. LiCari suspected the apple product to be a chemical substitute. His concern prompted him to tour the supplier's facilities, where he found only a warehouse. Mr. LiCari reported his findings internally to the organisation's Purchasing Manager and Vice President of Operations, neither of whom took any action in the matter. However, Mr. LiCari would not be discouraged, and eventually determined that the apple product was indeed false, and took his findings to the CEO who assured Mr. LiCari that he would investigate. Again, Mr. LiCari saw no action being taken. It seemed Beech-Nut's need to keep production costs down in the face of stiff competition outweighed the responsibility it owed to its consumers, and when no action had been taken after one year, Mr. LiCari left his job and reported what he knew to the U.S. Food and Drug Administration (FDA), who promptly launched a full enquiry. Mr. LiCari's actions were both responsible and justified, and he certainly explored all possible internal procedures. He was eventually forced by the refusal of his superiors to address a problem that was unethical, illegal and harmful to consumers

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to make his complaint to an external party whom he knew would take action. This is just one example of how whistleblowing can benefit society, by exposing the kind of careless risk an unethical organisation can place the public under, as well as helping to sustain or encourage an organisation's degree of social responsibility, through the threat of exposure.

Undoubtedly, whistleblowing also generates both negative and positive effects on the organisation. Once a whistleblower has disclosed to an external party, the public and media scrutiny, as well as possible resulting charges may result in long-term harm to the reputation of an organisation (Figg, 2000). As a consequence, an immense amount of time may be spent fighting whistleblower disclosures, resulting in a possible loss of morale among employees remaining within the organisation, and the formation of any chaos and mutual suspicion among employees can affect the performance of the organisation. There may also be issues of lost revenue and a decrease in the market performance of the organisation. Weinstein (1979 cited Keenan 1995, p.4) notes that more often than not, managers have taken the stance that whistleblowers pose a risk to the organisation's unification, authority structure, and public image.

Employees that blow the whistle externally are often forced to do so because their concerns are not given fair hearings by their employers, which may result in damage to both the whistleblower and the organisation. Yet if wrong doing within an organisation remains undetected, the result may create even greater damage to the workforce, and the public at large. No organisation is ever exempt from the general obligation it has to operate ethically, legally and with a good level of social responsibility. It is the failure of any type of organisation to fulfill these obligations that create the need for whistleblowing. If an organisation conducts its business in an ethical and responsible manner, then it has nothing to fear from whistleblowers (Figgs, 2003). Jones (1996) asserts that those that are "willing to risk reporting illegal and unethical behavior should be supported and protected".

Types of Whistle Blowing Activities carried out in an organisation

Whistleblowing action can be external, internal, personal and impersonal. It is internal when the whistle-blower discover misconduct in the workplace and communicate to people higher up in the organization who then follows established procedures to address the misconduct within the organization. External whistle-blowers are employees who discover corporate misconduct and choose to bring it to the attention of external parties, such as law enforcement agencies or the media. (Weiss, 2006). Effectiveness of whistleblowing likely varies, along with processes of retaliation, depending on whether whistleblowing is internal or external (Terry

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Dworkin, 1998). An employee's occupation in the organization likely impacts his or her choice of internal versus external channels for reporting wrong doing.

New employers are more likely to come out as a whistle-blowers in most of the organisations. During their work period they are less familiar with the appropriate channels and the environment of the organisation which they are working for (Miceli and Near, 1992). Less information on the firm's goal is disclosed to them in order for them to blow the whistle internally. Comparatively new employees may rely on external reporting channels because they identify themselves to be organizationally powerless. They may have contributed less in the organization, and be less concerned with stopping wrong doing in the way least harmful to the organization (Kolarska and Aldrich, 1980). They have less to lose because of their shorter tenure. Conversely, employees with longer contract in their organisation are more likely to feel some loyalty, leading them to use internal channels to report wrong doing.

Precluding the need for Whistleblowing

The act of whistleblowing is not something to be done without any suitable or acceptable justification. When blowing the whistle, consideration and certain approaches are to be taken in which whistle-blowing is morally justified. There are often personal obligations to family and others that may caught in an act against whistleblowing. One could be in the situation where blowing the whistle could result in job loss. However, the situation may take an unfortunate event and permanently blacklist an individual in his career, the sacrifice may become more than one's basic moral obligations require. (Schinzinger and Martin, 2000)

As a professional body, whistleblowing is morally honest and legal way to bring out the wrong doing in an organisation whether if they are big or small. It is important to explain that every employee has a role in preventing and detecting any wrong doings. However employees should consider or consult all the alternatives and choices before blowing the whistle. The moral justification is enforced if the whistle-blower has all relevant evidences and an understanding of any consequences. Their responsibility in view of their role within the organization should be clear. One should make sure that they have followed and apprehend the established procedures for whistleblowing, also that the repercussion that may cause inconveniences to other individuals. Whistle-blower's responsibility in view of their role within the organization should be clear and should provide strong evidence that can convince an impartial observer.

It is also recommended that employers develop an internal complaint system in which employees can report wrong doing. They may also credit employees for using the appropriate medium to investigate all wrong doings through superior in an organisation. Although whistleblowing may be anonymous, if it is to be effective

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it frequently requires not only that the whistle-blower reveal his or her identity, but also that he or she seek ways of publicizing the wrong doing. Because this may make the whistle-blower appear a self-appointed messiah, it prevents some people from speaking out. Detailed investigations may be more difficult, or even impossible, to progress if one choose to remain anonymous and cannot be contacted for further information. In a journal by Kroll and Egan, 2004, stated that to motivate an individual with a desire to do right, not wrong, the essential key is moral emotion. They also signifies that serving as a potential gateway from good intentions to good actions, much of the research in this domain has focused on negative valence and self-conscious emotions, such as, guilt and shame (Kroll & Egan, 2004).

The results from the above discussions support hypothesis that internal whistle-blowers were usually ineffective whistle-blowers, while external whistle-blowers often initiated investigations, helpful actions or other changes by the organization. Most ethicists agree whistleblowing is an ethical action. According to the Michael Davis, 1996 on whistleblowing, whistleblowing is morally required when it is required at all. Engineer have a moral obligation to prevent serious harm to others if they can do so with little costs to themselves.

In every organisations or corporation from government organisations to business establishments around the world whistleblowing has become a very important followed procedure. There has been heroic whistle-blowers world over. Ernest Fitzgerald and the C-5A, and Edward Snowden are few whistle-blowers who came forward with what they thought was a right approach to take.

There is no denying the fact that whistle-blowers do a great service to the society at their great risk and cost, even at the loss of life. Any individual can raise concerns about any issue relating to suspected misconduct at work place, risk to any employees, abuse or wrong doing. If they have a reasonable certainty that the problem has taken place, is taking place or will presumably take place in the future. Employee may have doubt or may be frightened to raise a concern even when legal protection exists. Employees can be advised to raise a concern openly, confidentially or anonymously.

They should be made aware of certain solution as to raise any concern as early as possible no matter how big the suspicion maybe, this allows the matter to be looked into promptly. Employers in any company are thought to be responsible for their actions and one way to do so is to encourage whistleblowing if wrong doing is witnessed. In conclusion, whistleblowing is an essential practice in any organisation which is very vital for them to protect from fraud, corruption and wrong doing.

Sneha Dutta
Department of Business Administration
Asutosh College

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Sneha Dutta
Department of Business Administration
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