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# **A REVIEW ON CADBURY REPORT**

**Prepared By: JST 2014**



# Introduction

- The Cadbury report was once referred to as The Report of The Committee on the Financial Aspects of Corporate Governance. The report was published in December 1992, following the recommendations of the Cadbury Committee.
- Address concerns about the working of the corporate governance system.
- The Committee made it its purpose to address the financial aspects of corporate governance and out of this produced a Code of Best Practice.

# The Committee

- The Cadbury Committee was established in May 1991 by the Financial Reporting Council, the London Stock Exchange, and the accountancy profession.
- **Reasons:**
  - Increasing lack of investor confidence in the honesty and accountability of listed companies.
  - Financial collapses of listed corporations.
  - Auditors who signed off a set accounts which turned out be a misrepresentation of the facts, and about losing its self-regulatory role.
  - Lack of board accountability for such matters as directors' pay.

# Corporate Governance

- Contemporary corporate governance started in 1992 with the Cadbury report in the UK
- Cadbury was the result of several high profile company collapses
- is concerned primarily with protecting weak and widely dispersed shareholders against self-interested Directors and managers

# Cadbury Report 1992

- The committee on the financial aspects of corporate governance'
- The Code of Best Practice' (1992)
  - Voluntary code
    - But for listed companies a compliance statement was required
      - 'Comply or explain' – *Principles rather than rules*
        - The 'principles v rules' argument (UK v USA)
        - The following example is a true case, but in a non-financial setting (from China Daily, December 2007)

# Corporate Governance Parties

- Shareholders – those that own the company
- Directors – Guardians of the Company's assets for the Shareholders
- Managers who use the Company's assets

# Corporate Governance

- Primarily concerned with public listed companies i.e. those listed on a Stock Exchange
- Focused on preventing corporate collapses such as Enron, Polly Peck and the Maxwell companies

# Corporate governance based on Africa

- What relevance does it have to Africa where there are few public listed companies
- Most companies are non-listed, private family owned businesses where the shareholders and the managers are often the same people

# Four pillars of Corporate Governance

- Accountability
- Fairness
- Transparency
- Independence

# Accountability

- Ensure that management is accountable to the Board
- Ensure that the Board is accountable to shareholders

# Fairness

- Protect Shareholders rights
- Treat all shareholders including minorities, equitably
- Provide effective redress for violations

# Transparency

- Ensure timely, accurate disclosure on all material matters, including the financial situation, performance, ownership and corporate governance

# Independence

- Procedures and structures are in place so as to minimize, or avoid completely conflicts of interest
- Independent Directors and Advisers i.e. free from the influence of others

# Cadbury Report 1992

- This, more than any other initiative in corporate governance reform, has led to the shift of directors' dialogue towards greater accountability and engagement with shareholders...' and
- '...has generated the more significant change of corporate responsibility toward a range of stakeholders, encouraging greater corporate social responsibility in general'

Solomon, 2007

# CONT'D.....

- The report covered three areas
  - **Directors**
    - *It defined the composition of the board, its responsibilities, and the responsibilities of the chairman, and the audit and remuneration committees.*
  - **Auditing**
  - **Shareholders**



**'Fat cats'**



# Corporate Governance in Africa

- In 1994, The King Report in South Africa also included within its Code of Corporate Governance requirements on sustainability and ethical standards
- This was due to the context of a developing country and business ethics in Africa

# Stakeholders

- Sustainability recognizes stakeholder rights i.e. the rights of interested parties e.g. employees, the community, suppliers, customers etc.
- Encourage co-operation between the company and its stakeholders in creating wealth, jobs and economic stability

# **According to Cadbury Report on Corporate Governance should based on:**

- Good Board practices
- Control Environment
- Transparent disclosure
- Well-defined shareholder rights
- Board commitment

# Strengths

- Creates confidence among the shareholders, customers & suppliers, etc...
- Improves leadership
- Demonstrating transparency, integrity & social accountability
- The provisions of the Code were given statutory authority to the extent that the London Stock Exchange required listed companies to 'comply or explain'
- The Cadbury Report quickly proliferated and became internationally influential.
- It triggered successive waves of rethinking.

# Critique and Dilemmas

- Not mandatory.
- Executive pay and perks.
- Internal auditors.

## **Weaknesses**

- It was costly to implement as the cost of was estimated to be at least 10% of the annual audit fee.
- The Stock Exchange quickly made it clear that it was not inclined to delist those companies who refused to implement the codes, companies were under no obligation to enforce them

# Validity of the report

- The Cadbury report proved to be a strong turn-around strategy for the UK economy.
- The Cadbury Report, a “code of best practice” which served as a basis for reform of corporate governance around the world.
- Today it serves as a crucial report in Corporate Governance Literature that is ground breaking in corporate governance.
- Has given light and emerged a better comprehension on the issues of accountability, openness and Integrity.

# Conclusion

- The Cadbury Report was followed by three more major reports:
  - Greenbury (1995),
  - Hampel (1998) and
  - Turnbull (1999).
- Compliance with the Code of best Practice was not enforced and it was not mandatory. However, many firms conformed because they did not want to fall victim to the destructive consequences resulting from the disregard of corporate governance.