

Report role corporate government

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Submission date: 05-Jul-2023 01:41PM (UTC+0100)

Submission ID: 209855283

File name: 27735_Barbara_Berto_Report_role_corporate_government_504416_1975522864.docx (24.17K)

Word count: 1931

Character count: 12653

Module: LCBB6002 IFM Com 1

**A Report on
The Role of corporate governance and how it
contributed to the Lehman Brothers financial
crisis in 2008**

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Executive summary

It provides an overview of the discussion on the impact that corporate governance flaws had on the failure of Lehman Brothers during the global financial crisis in 2008, and it does so by focusing on the implications of those flaws. Inadequate risk management practices, ineffective board oversight, a lack of transparency, and conflicts of interest are some of the key findings that are highlighted. These flaws in the corporate governance framework of Lehman Brothers contributed to the company's demise and highlighted more extensive systemic failures in the financial sector. The report stresses the importance of good corporate governance, regulatory reforms, and improved risk management in avoiding future crises and stabilising the economy.

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Introduction

Corporate governance is crucial in deciding how organisations operate and behave while fostering transparency, accountability, and moral decision-making. It contains all the mechanisms, protocols, and linkages needed to direct and oversee businesses (Aras, 2017). Following the global financial crisis in 2008, corporate governance was recognised as a critical element that led to the instability of financial organisations, notably the famed Lehman Brothers. The international economy was profoundly affected by the global financial crisis 2008, which was characterised by a widespread collapse of financial markets and institutions. Excessive risk-taking, weak regulatory frameworks, and subpar corporate governance procedures exacerbated the crisis. In this case, the problem was caused mainly by the collapse of the renowned investment bank Lehman Brothers. Due to inadequate risk management practises and weak board monitoring, Lehman Brothers' fall exposed severe corporate governance flaws (HBS Baker Library, 2018). The bank's colossal debt, complex financial instruments, and aggressive pursuit of short-term returns increased its risk. Poor transparency and disclosure practices concealed the bank's financial predicament, deceiving authorities and investors. The failure of Lehman Brothers served as a wake-up call, highlighting the essential need for good corporate governance practises across the banking sector. It triggered extensive changes to enhance corporate responsibility, risk management, and governance. Decision-makers and market participants sought to avoid similar crises and improve long-term financial stability by learning from past mistakes and enhancing corporate governance norms (Clein, 2020). This study investigates how corporate governance contributed to the crisis and how those significant governance weaknesses affected Lehman Brothers' downfall.

Overview of Lehman Brothers' Corporate Governance Errors

The shortcomings in corporate governance substantially impacted the failures observed during the 2008 global financial crisis, particularly in Lehman Brothers. Lehman Brothers' demise during the global financial crisis in 2008 was greatly affected by the faults in corporate governance. Lehman Brothers' collapse was caused by several aspects of its corporate governance framework, including poor risk management procedures, ineffective board oversight, and a lack of transparency.

First, Lehman Brothers' poor risk management procedures were a significant factor in its demise. The business adopted aggressive tactics and invested significantly in complicated financial products like mortgage-backed securities. However, it needed to evaluate and manage the present risks adequately. Excessive exposure to subprime mortgages and other high-risk assets resulted from the risk management framework's lack of reliable mechanisms to detect and reduce potential threats (Mallin, 2019). Second, risky practices at Lehman Brothers were allowed to continue because the board's oversight was ineffective. The board of directors needed to challenge management choices or the company's business strategy adequately. Due to the absence of independent oversight, serious risks must be adequately managed, and early signs of trouble were disregarded. Lehman Brothers' failure was primarily caused by the board's serious flaw in corporate governance, which was its failure to uphold its fiduciary responsibility and provide efficient governance oversight (Lioudis, 2021). Failures in transparency and disclosure contributed to the demise of Lehman Brothers. The financial statements and revelations of the company could have fairly depicted its actual financial situation. Lehman Brothers concealed its excessive leverage and risk exposure using dubious accounting techniques, such as off-balance-sheet entities. This lack of transparency misled investors, regulators, and other stakeholders, making it impossible for them to thoroughly comprehend the firm's precarious financial situation. Lehman Brothers' corporate governance structure contained conflicts of interest that hurt how decisions were made. The business had strong ties to the mortgage sector thanks to its work securitising and originating subprime mortgages. This led to tensions between the company's desire for profit and its obligation to act in the best interests of its stakeholders. Lehman Brothers' governance structure was further weakened by an inability to resolve these conflicts of interest.

Lehman Brothers' corporate governance flaws were not isolated incidents; instead, they were a symptom of more widespread systemic problems in the financial sector. The crisis revealed

significant oversight gaps and the need for improved corporate governance procedures everywhere(Saif,n.d.). Regulators, decision-makers, and market participants reviewed and strengthened corporate governance standards in response to the failures at Lehman Brothers to avert similar crises in the future.

To increase risk management and corporate governance practises in the banking industry in the wake of the crisis, rules were amended. Enhancements to board independence, transparency, and risk management are made through these reforms. They included both national rules like the Dodd-Frank Act and international frameworks like Basel III. Lehman Brothers' fall and the more extensive 2008 global financial crisis were both impacted by poor corporate governance. Fundamental governance difficulties for the corporation were a lack of transparency, conflicts of interest, ineffective risk management procedures, and insufficient board monitoring. The current financial crisis served as a wake-up call, stressing the need for more excellent regulatory monitoring and more robust corporate governance practises to safeguard the financial system's stability.

Analyzing the Effect of Corporate Governance Defects on Lehman Brothers' Failure During the Global Financial Crisis of 2008

According to the study, inadequate corporate governance substantially impacted Lehman Brothers' failure during the 2008 global financial crisis. Lehman Brothers' deficient corporate governance, which was typified by, among other things, a lack of transparency, conflicts of interest, and insufficient risk management practises, is credited as contributing to the company's failure.

The failure of risk management standards significantly impacted Lehman Brothers' financial collapse. The corporation was exposed to severe challenges due to its audacious business plans and significant investments in sophisticated financial instruments. Due to the inability of the risk management framework to accurately assess and mitigate the risks involved, high-risk assets, including subprime mortgages, were left with an excessive amount of exposure (Gordon and Ringe, 2018). Due to this flaw, it is clear how important it is for financial institutions to have efficient

risk management procedures to protect themselves from severe economic downturns. The inadequate board oversight that was in place at Lehman Brothers was another significant factor that contributed significantly to the company's demise. The company's board of directors did not adequately challenge the management's decisions or question the company's business model. Serious threats were not identified or addressed because there was insufficient objective oversight (Berhe, 2023). The significance of an attentive and involved board in the corporate governance is demonstrated by its failure to fulfil its fiduciary responsibility.

The failure of Lehman Brothers to be transparent and disclose information also contributed to its downfall. The company's financial statements and disclosures did not accurately represent the company's actual financial situation. Lehman Brothers used questionable methods of accounting, such as off-balance-sheet entities, to hide the excessive leverage and risk exposure that the company was exposed to (UpCounsel, n.d.). As a result of this lack of transparency, investors, regulators, and other stakeholders were led astray, and they needed help understanding the precarious financial situation the company was in. The analysis highlights the necessity of being transparent and making accurate disclosures to guarantee that decisions are made based on accurate information.

The corporate governance structure of Lehman Brothers was riddled with conflicts of interest, which made decision-making more difficult. Conflicts arose within the company due to its close ties to the mortgage industry between its desire to profit and its obligation to act in the best interests of its shareholders and other stakeholders (Larcker and Tayan, 2020). The inability to effectively manage these conflicts of interest made the governance structure even more fragile. This finding highlights how important it is to address conflicts of interest in order to keep the credibility of corporate governance intact.

The analysis concludes that systemic failures in the financial industry, rather than isolated incidents, were to blame for the weaknesses in Lehman Brothers' corporate governance. The crisis highlighted the need for improved corporate governance procedures and exposed significant oversight gaps (www.oecd.org, n.d.). Regulatory reforms like the Dodd-Frank Act and the Basel III framework were introduced to improve risk management in financial institutions and strengthen corporate governance standards. The analysis emphasises how crucial corporate governance is to maintaining financial stability. The weaknesses in its corporate governance architecture, including risk management, board monitoring, transparency, and conflicts of interest,

impacted Lehman Brothers' demise and the more serious global financial crisis 2008. Regulation monitoring and corporate governance practise are being improved to maintain the financial system's stability and avert future problems.

Conclusion

The bankruptcy of Lehman Brothers in the 2008 global financial crisis played a crucial part in poor corporate governance, which is highlighted in the discussion. Ineffective board monitoring, a lack of transparency, conflicts of interest, and poor risk management practices were the main factors leading to the firm's demise. These weaknesses affected other companies outside Lehman Brothers, exposing more pervasive systemic flaws in the banking industry. The study emphasises how important it is for corporate governance to have robust risk management, independent board monitoring, transparency, and effective conflict management. Lessons learnt from the crisis have sparked attempts to tighten corporate governance practises, alter regulations, and increase regulatory monitoring to avert future disasters. Improving corporate governance norms and procedures is crucial to sustain financial stability and prevent systemic risks. By addressing these shortcomings, businesses and regulators may strengthen the foundation for moral judgement, transparency, and accountability in the financial industry. The discussion emphasises how crucial it is to keep enhancing corporate governance to safeguard the financial system's stability and lessen the likelihood of future crises.

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