

# **CORPORATE GOVERNANCE AND ETHICAL STANDARDS IN BUSINESS: THE UGANDAN EXPERIENCE**

*By*

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## **Abstract**

*Ethics in corporate governance is very important as it gives companies focused and purposeful management, and a competitive edge in business. This is the first installment of a study of legislation and other literature relating to ethics and governance specific to Uganda. In this research the factors affecting good business ethics is considered, as well as the opportunities arising from good ethical practices. The study's findings indicate that there are several factors affecting ethics in corporate governance in Uganda. These include the company's internal environment, and the external environment because the company does not operate in a vacuum. Factors in the external environment include the socio-political, cultural and market environments, and the legal environment as well as regulatory environment. The main factors affecting good business ethics in Uganda are in the context of the socio-political environment. This study contributes to the drive by policy-makers towards promoting good corporate governance by drawing attention to the main factors affecting good business ethics in Uganda.*

**Keywords:** Ethics, corporate governance, Uganda

## **Introduction**

There is no standard definition of corporate governance. However, it has been defined to mean the systems by which companies are governed and controlled.<sup>1</sup> On the other hand Ethics refers to that which is good or right in human interaction, and it involves 'self', 'good', and 'other'.<sup>2</sup> Thus, one is said to have acted ethically if he considers not only what is good for

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<sup>1</sup>Report of the Committee on the Financial Aspects of Corporate Governance: The Code of Best Practice (Cadbury Code) (1992).

<sup>2</sup>King Code of Corporate Governance for South Africa p. 51.

him, but also what is good for *others*.<sup>3</sup> Business ethics refers to the ethical values that determine the interaction between a company and its stakeholders,<sup>4</sup> who include the customers, suppliers, and employees among others. In recent times, corporate governance has become a subject of great importance and discourse, because there have been corporate collapses brought on due to ethical failure. Examples of ethical issues in corporate governance include misreporting, excessive remuneration<sup>5</sup>, concealment of revenues, taking bribes, conflicts of interest, and insider trading among others. This article seeks to show that ethics is important in corporate governance, and explores the factors that influence the practice of good governance.

### **The Importance of Business Ethics**

Good business ethics firstly, promotes the company's profitability. The reason is that a greater attention to morality attracts customers or clients, because of a good reputation, and this in turn, leads to a higher profit,<sup>6</sup> when they purchase the company's goods or services. On the other hand, unethical practices manifesting in fraud result in financial loss to enterprises.<sup>7</sup> Financial loss may be incurred because 'unethical behavior may lead to an increase in operational, legal, marketing and public relations costs'.<sup>8</sup>

Secondly, business ethics boost the production process because it leads to better utilization of resources, environmental protection, cleaner production and energy conservation.<sup>9</sup> It also 'lead[s] to happier suppliers of services such as raw material and

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<sup>3</sup>*Ibid.*

<sup>4</sup>*Ibid.*

<sup>5</sup>Business Ethics Presentation on Slide share available on [http://www.slideshare.net/y4ss1r/business-ethics-14811885?next\\_slideshow=1](http://www.slideshare.net/y4ss1r/business-ethics-14811885?next_slideshow=1) accessed on the 5<sup>th</sup> August 2015.

<sup>6</sup>Birungyi Cephas Kagyenda, Business Ethics, *Wealth Creation Journal* Vol. IV 2007 p.8.

<sup>7</sup>Leo Kibirango, 'Business Ethics- A Necessity' *Sustainable Wealth Creation Journal* Vol. IV 2007 p. 6.

<sup>8</sup>See also John Graham, The Role of Corporate Culture in Business Ethics p. 389 available at [http://www.cutn.sk/Library/proceedings/mch\\_2013/editovane\\_prispevky/44.%20Graham.pdf](http://www.cutn.sk/Library/proceedings/mch_2013/editovane_prispevky/44.%20Graham.pdf) on 31<sup>st</sup> July 2015.

<sup>9</sup>Jane Gitau, Ethics in Business - A Foundation for Economic Growth, *Sustainable Wealth Creation Journal* Vol. IV 2007 p. 11 citing Dr. Maggie Kigozi.

packaging<sup>10</sup> because suppliers will be assured that they will be paid. The production process is also boosted because good ethics attracts good and talented employees to work in the company,<sup>11</sup> which will in turn lead to increased productivity of the company. In this respect, it encourages persons with high ethical standards to work in a way that is consistent with their sense of right and wrong. Pressuring people to work contrary to their convictions places them in a place of a great deal of emotional stress, hereby decreasing their work output levels. In addition, good ethics provide multiple channels of feedback,<sup>12</sup> because the stakeholders trust the company. Feedback is useful to a company because it enables the company to address issues that if addressed adequately, could improve the company's performance.

Thirdly, is that it attracts capital. The reason is that the practice of good ethics attracts investments at much lower costs because fraud and corruption are checked out altogether.<sup>13</sup> It also promotes trust between companies, and so encourages business partnerships and alliances<sup>14</sup> which increases the accessibility to capital. From the above, it is clear that it is in a company's best interests for the company's officials to practice good ethics, for the sustainable success of its business.

### **Factors Affecting Company's Ethical Practices**

Company officers do not operate in a vacuum. The Environment in which the company operates can affect the ethical environment within the company. Environment means the surrounding circumstances, background, or context in which the company's officers operate. These may be internal environment factors and the external environment. The former includes the

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<sup>10</sup>Ibid.

<sup>11</sup> 'Ethical business practices A Cadbury Schweppes case study' available at: <http://businesscasestudies.co.uk/cadbury-schweppes/ethical-business-practices/the-importance-of-ethics-in-business.html#ixzz3XY9pRLiM> accessed on the 17<sup>th</sup> April 2015.

<sup>12</sup>Birungyi Cephas, *Supra* p.8.

<sup>13</sup>Jane Gitau, *Supra* p. 10 citing Charles Muchene, the Country Leader Price waterhouse coopers by 2005.

<sup>14</sup>*Business Ethics* p. 32 available at

[http://www.google.co.ug/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=0CB0QFjAA&url=http%3A%2F%2Fhighered.mheducation.com%2Fsites%2Fdl%2Ffree%2F0070921989%2F226745%2Fferrell\\_sampleCH02.pdf&ei=kbUwVZm2M6ep7Abhx4CwBw&usg=AFQjCNEwKtLUFSzl566sHUXSc39p0eLXQacc](http://www.google.co.ug/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=0CB0QFjAA&url=http%3A%2F%2Fhighered.mheducation.com%2Fsites%2Fdl%2Ffree%2F0070921989%2F226745%2Fferrell_sampleCH02.pdf&ei=kbUwVZm2M6ep7Abhx4CwBw&usg=AFQjCNEwKtLUFSzl566sHUXSc39p0eLXQacc) accessed on 17<sup>th</sup> April 2015.

company's internal environment and the latter includes the market environment, the socio- political environment, and the legal and regulatory environment. The discussion will commence with the internal environment.

### a. Ethics and the Company's Internal Environment

This has to do with whether or not a company has a culture of integrity and transparency. Where the corporate culture fosters integrity, then there is likely to be greater application of business ethics in the company. Where for example transparency is promoted in the company, unethical practices are unlikely to thrive. The degree of internal supervision of management by the board is also critical towards determining whether there is a culture of ethical business practices. Research studies have shown that where there is poor management oversight by the board of directors, corporate scandals are more likely to thrive.<sup>15</sup> This means that poor corporate governance enables the company's management to make unethical decisions.<sup>16</sup> Thus, where there is good corporate governance, the management of the company will ensure that there is transparency, and accountability.<sup>17</sup>

Also, the performance philosophy within the company affects the ethical climate of the company. The performance philosophy refers to the emphasis placed by the company's management on the employees, as to where their energies ought to be expended. Where the culture is geared towards individual performance and profits, poor ethics will thrive. On the other hand,

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<sup>15</sup>Hoffman, Rowe, The Ethics Officer as Agent of the Board: Leveraging Ethics Governance Capabilities in the Post Enron Corporation Business and Society Review 112:4 , 553- 572 cited in p.2. Yasemin Zengin Karaibrahimoglu, Burcu Guneri Cangarli, *Do Auditing and Reporting Standards Affect Firms' Ethical Behaviours? The Moderating Role of National Culture* Journal of Business Ethics 2015 available at [http://download.springer.com/static/pdf/439/art%253A10.1007%252Fs10551-015-2571-y.pdf?originUrl=http%3A%2F%2Flink.springer.com%2Farticle%2F10.1007%2Fs10551-015-2571-y&token2=exp=1438333007~acl=%2Fstatic%2Fpdf%2F439%2Fart%25253A10.1007%25252Fs10551-015-2571-y.pdf%3ForiginUrl%3Dhttp%253A%252F%252Flink.springer.com%252Farticle%252F10.1007%252Fs10551-015-2571-y\\*~hmac=060637490e4302656d2fb8925925421d9645defd06a1b33fc1b340e2d3df15ff](http://download.springer.com/static/pdf/439/art%253A10.1007%252Fs10551-015-2571-y.pdf?originUrl=http%3A%2F%2Flink.springer.com%2Farticle%2F10.1007%2Fs10551-015-2571-y&token2=exp=1438333007~acl=%2Fstatic%2Fpdf%2F439%2Fart%25253A10.1007%25252Fs10551-015-2571-y.pdf%3ForiginUrl%3Dhttp%253A%252F%252Flink.springer.com%252Farticle%252F10.1007%252Fs10551-015-2571-y*~hmac=060637490e4302656d2fb8925925421d9645defd06a1b33fc1b340e2d3df15ff) accessed on the 30<sup>th</sup> July 2015.

<sup>16</sup>*Ibid.*

<sup>17</sup>*Ibid.*

where good corporate citizenship is emphasized in addition to profit, better ethical standards will be observed. Two examples involving Enron, and Wall-Mart will suffice in to illustrate this point. With respect to Enron, its internal culture was to reward individual raw talent.<sup>18</sup> that increased the company's profits. This gave opportunity for fraud to thrive, because the company's employees were put under pressure to deliver results at all costs regardless of the means they applied to achieve their targets. Every year there was a compulsory laying off of employees so there was overwhelming pressure to perform. On the other hand, is Wall-Mart, the world's largest company, in terms of revenues and number of employees, whose core values are devotion to customers, and valuing team results more than individual results.<sup>19</sup> It is not surprising that Wall-Mart has survived longer in business it is opined, largely because of its corporate culture in this regard.

### **b. Ethics and the Company's External Environment**

The external environment includes the market environment, the socio-political environment, and legal and regulatory environment.

### **c. The Socio-Political, Cultural and Market Environments**

Culture is 'a set of societal values that drive institutional form and practice'<sup>20</sup> or 'the collective programming of the mind which distinguishes the members of one human group from another',<sup>21</sup> and it provides the cognitive terms for individuals

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<sup>18</sup>Justice Geoffrey Kiryabwire, 'Business Ethics in Uganda: time to walk the talk?' *Capital Markets Industry Journal* July- December 2011 p. 34.

<sup>19</sup>*Ibid.* See also Alexander Crofoot Wal-Mart: Rolling Back on Ethics available at <http://www.neumann.edu/academics/divisions/business/journal/Review2012/Crofoot.pdf> accessed on the 3<sup>rd</sup> September 2015 where that author notes that Walmart has also been the center of ethical controversies. However, it is opined that compared to Enron, Walmart has fared better although it is by no means perfect.

<sup>20</sup> Salter and Niswander, "Cultural Influence on The Development of Accounting Systems Internationally, a Test of Gray's (1988) Theory", *Journal of International Business Studies*, Second Quarter, 1995 p.149 cited in Cigdem Solas, Sinan Ayhan, The Historical Evolution Of Accounting In China: The Effects of Culture *Spanish Journal of Accounting History* No.7 (December 2007) p.149.

<sup>21</sup> Hofstede, G. 1980. Culture's consequences: International differences in work-related values. London:

Sage Publications cited in Nigel Finch, Testing The Theory Of Cultural Influence

within a group and society preconditions for human behavior.<sup>22</sup> The culture of the society in a particular country may have an impact on corporate culture of a company, because it has a direct impact on the behavior of individual directors or management of the company. The socio-political environment includes the moral state of the society, and attitude of the political leadership towards promoting and upholding ethics in the society. Where a society is characterized by poor morals like corruption, company officials are more likely to practice poor ethics.<sup>23</sup> In Uganda over the years there has been a decline in the morals of society especially manifesting in personal and corporate greed<sup>24</sup>, materialism,<sup>25</sup> short-term gains mentality, the pressure to deliver

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On International Accounting Practice *Allied Academies International Conference* p.27.

<sup>22</sup>Gao, Simon S. – Handley Schachler, Morrison.: The Influence of Confucianism, Feng Shui and Buddhism in Chinese Accounting History, Accounting, Business & Financial History, Volume 13, 1 March 2003, (Çevrimiçi)

www.taylorandfrancis.metapress.com/index/0L0UJH89A2LYRMBQ.pdf,03.06.2006 cited in Cigdem Solas, Sinan Ayhan, The Historical Evolution Of Accounting In China: The Effects of Culture *Spanish Journal of Accounting History* No.7 (December 2007) p.151.

<sup>23</sup>See Simeon Wanyama, 'Corporate Governance and Accountability in Uganda : An Analysis of Stakeholder Perspectives' (2006) ( Phd Thesis at the University of Dundee) at p. 103.

<sup>24</sup>Justice Geoffrey Kiryabwire, *Supra* where that author mentions criminal greed, cultural tradition (at p. 33) , failure to observe the basic principles of good corporate governance, and corporate ethical behavior (p. 34).

<sup>25</sup> Haji Ahmed Ahmed, 'Ethics? What's it?' *Wealth Creation Journal* Vol. IV 2007 p.25 at 28. See also Lajul Wilfred, *Impact of African Traditional Ethics on Behaviour in Uganda*, in MAWAZO: The Journal of Humanities and Social Sciences, Makerere University, Vol. II No. 1 April 2011, (p.131) Makerere University Printer, Kampala, who argues that in Uganda moral decline is manifested by the use of the end justifying the means, and the use of Machiavellian theories which state that politics ought not be subjected to morals or else leaders will be weak. He also argues that in Uganda people who amass wealth are seen to be heroes, while those who amass wealth slowly are considered fools. He also argues that allegiance to families may encourage corruption because decisions may be made in the interests of tribal allegiance as opposed to the best interests of the corporation. Simeon Wanyama, *supra* at p. 14 notes that tribal allegiances ' may lead to conflicts between acting in the best interests of the company or institution where one works, or fulfilling the tribal, clan or family expectations. Some officials may end up in unethical practices in order to raise money to satisfy these expectations'.

and absence of a sufficient number of good role models.<sup>26</sup> It can, therefore, be inferred from this that company officials are more prone to unethical practices today than before. Also, where there is a poor ethical culture in society, it affects the regulators' ability and willingness to give oversight of companies and the different players in the economy. Similarly, it affects the ability of different gatekeepers to play their watchdog role effectively since they themselves will be inclined to act unethically, being part of the society.

Where there is a lack of political will against corruption there will be an environment in which good ethical practices in business are discouraged, while on the other hand, bad ethical practices go unchecked or are given occasion to thrive. On the other hand, where there is strong political will to fight bad ethics, good ethics in corporate governance will be encouraged to thrive.<sup>27</sup> It has been observed that in Uganda there has been a lack of a sufficient political will to fight corruption,<sup>28</sup> which it is opined, encourages bad ethics in corporate governance in the country. With respect to the marketing environment, the environment in which the companies carry out business is also important, for example in an environment where bad competition practices are allowed there will be a great deal of unethical practices allowed to be perpetuated.<sup>29</sup>

#### **d. The Legal and Regulatory Environment**

The legal and regulatory environment includes the legislation regulating corporate governance and legal reprisals or liability resulting from the abuse of those laws and regulations. A key factor closely related to the risk of liability is the efficiency of the legal system, because if the legal system is characterized by

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<sup>26</sup>Jane Gitau, *Supra* at p. 11 citing Charles Muchene, the Country Leader Price water house coopers by 2005.

<sup>27</sup>Justice Geoffrey Kiryabwire, *supra* p. 37. See also Birungyi Cephas *supra* p.7 where that author discusses cultural attitudes concerning eating beef, dogs and western countries who have zero tolerance for corruption. That author also suggests that poverty may contribute to increased corruption in a society.

<sup>28</sup>Simeon Wanyama, *supra* at p.176 footnote 136.

<sup>29</sup>Kimera Henry Richard, *Competition Regimes in the World- A Civil Society Report* ( Uganda ) ( CUTS International) p. 297.

swift penal action against errant directors or managers, there will be a deterrent against bad ethical practices. This is more so where there is lack of rule of law, and in this respect the environment may not be very favorable in Uganda since there are concerns about a massive case backlog in the courts of judicature, which may hinder the effectiveness and efficiency of the legal system especially in the handling of commercial disputes.

## **Conclusion**

Ethics in business is important but factors both internal and external to the company have the effect of increasing the likelihood of unethical practices being perpetuated within the company. Any measures to improve the practice of ethics in corporate governance ought to take into account the above threats to ethical practices. The next article will address measures that may be taken to addresses these hindrances to good ethics, in the context of Uganda.



