

ETHICS AND ETHICAL PRACTICES IN BANKS: A REVIEW OF LITERATURE

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Abstract *This paper presents a comprehensive review of literature on ethics, ethical issues, and ethical practices in the banking industry. This review paper will help in understanding ethics and ethical practices in banks, and will build a roadmap for future research in this area. Articles are downloaded from PROQUEST, Researchgate, EBSCO, and other online sources. Keywords used for search were banks and ethics, ethics in banks, ethical issues in banks, factors of bank ethics, and bank failure and ethics. The review of literature revealed that there are numerous ethical issues prevalent in the banking industry, like lack of proper ethics training, trust and transparency issues, growing pressure of competition, complexity of banking operations, issue of money laundering, and so on. It is observed that factors that affect ethics in banks include internal behaviour, cost leveraging, value leveraging, ethical orientation, ethical lending, ethical commitment, placement of assets, ethical ideology, bank's code of conduct, and so on.*

Keywords *Banks and Ethics, Ethics in Banks, Ethical Practices, Ethical Issues, Factors of Bank Ethics*

INTRODUCTION

Ethics is built on fair work practices, right decisions, and doing what is morally right. It outlines general guidelines and perceptions on good conduct/behaviour of individuals, groups, and organisations as a whole. Ethics and ethical issues have become a burning topic for corporates and academicians worldwide. Ethics and ethical practices are all the more significant in the banking industry, as the economy of a country is solely dependent on this sector.

Banks are not only supposed to function competently, but transparently and ethically so that the people continue to have confidence in the system. Banking ethics is all about faithfulness and honesty to customers and other stakeholders, impartiality, trustworthiness, valuing principles, and working with a high degree of transparency. A number of deficiencies are found in the banking system due to unethical banking activities, which are evidenced by a number of studies conducted by various committees appointed by the government and RBI in India, such as Talwar Committee (1975), Goiporia Committee (1990), Tarapore Committee (2004), Sadasivan Working Group (2006), and so on. Researchers across the globe have also explored ethics in the banking sector.

The objective of this paper is to review the literature related to ethics and ethical practices in the banking sector. This will lead to an understanding of the ethical practices and related issues in the banking sector. The paper is organised as follows:

- Introduction
- Ethical issues in banks
- Factors affecting ethics in banks
- Ethics in banks
- Ethics and bank failure
- Conclusion

ETHICAL ISSUES IN BANKS

Harris and Spence (2002) examined the ethics of business-to-business electronic commerce in the banking sector. The key areas identified were trust and transparency of business-to-business transactions, freedom of choice, and limits to accountability with regard to the facilitation of deceit. Yidawi (2005) examined a number of problems and ethical issues in the banking sector in Nigeria and found that the major issues were lack of qualified skilled bankers, breaking of Central Bank of Nigeria (CBN) and Nigeria Deposit Insurance Corporation (NDIC) guidelines, lack of proper ethics training, frauds, and other malpractices. Goyal and Joshi (2011) focused on historical background, past performances and development, and social and ethical issues relating to the Indian banking industry to highlight issues such as social banking, green banking, ethical banking, rural banking, global banking, and agro-banking. These issues were found to be helpful in achieving sustainable development of finance and banking. It was suggested that banks could portray themselves as a socially and ethically oriented institute by disbursing loans to projects with a concern for

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the environment. Senthikumar et al. (2011) observed that the quality and ethical values of banks has been dazed because of the growing pressure of competition, as well as meeting the high expectations and demands of the customers. The presence of a large number of banks and their branches all over the country, revolution of e-banking, availability of multiple products and services, and an increase in the number of bank customers has resulted in complexities in banking operations. Fetinuic (2014) found that the problems of abusive behaviour of banks were mostly attributable to the principles of self-interest, unethical corporate administration of top banks, and faulty consumer rights legislation in the banking sector. It was found in the research that the issue of money laundering was prevalent globally, bringing severe damage to the health of the banking industry, their image, and experience, hazarding serious sanctions from the control bodies.

Table 1: Studies on Ethical Issues in Banks

Author	Year	Sample	Findings (Issues Identified)
Harris & Spence	2002	United Kingdom	Trust & transparency of business, freedom of choice & accountability
Yidawi	2005	Nigeria	Lack of qualified bankers, breaking of guidelines, lack of proper ethics training, frauds & other malpractices
Goyal & Joshi	2011	India	Issues identified for focus – social banking, green banking, ethical banking, global banking & agro banking
Senthikumar	2011	Chennai, India	Growing presence of competition, meeting high expectations & demands of customers, complexities of bank operations
Fetinuic	2014	Republic of Moldova	Self-interest, unethical corporate administration, money laundering

FACTORS AFFECTING ETHICS IN BANKS

Mitchell (1992) found that there were 17 categories of ethical behaviour in banks, and that they were related to internal behaviours. The study found that younger employees had a higher level of ethical consciousness than older employees. In addition, it was observed that the longer one worked for an organisation, the more one is likely to take job security as a priority; this could lead to overlooking or rationalising unethical behaviours. The author further suggested that more emphasis was needed on internal behaviours, particularly on the impact that external behaviours had on the former.

Božović (2007) highlighted business ethics as a social responsibility of an individual, as well as of joint moral actions followed during all aspects of business dealings. It was concluded in the study that the application of a code of ethics helps establish a defensive mechanism in the field of ethical values application. Chowdhury (2011) conducted a research to find the principle factors of ethical practices in order to develop a model for competitive advantage in banking. The study found two principle factors during analysis, namely, the cost leveraging factor and the value leveraging factor, which result in competitive advantage. Moreover, it was observed that high ethical practice leads to high customer satisfaction and performance. Icke et al. (2011) emphasised that avoiding social exclusion and placement of assets were major factors that differentiated ethical banks and other financial institutions. Jose et al. (2011) studied the differences between traditional financial intermediaries and ethical banks based on property rights. They focused on an index, called the Radical Affinity Index (RAI); they hoped to differentiate ethical banks from other banks, and also to identify the differences between the various ethical banks themselves. This index grouped banks together in terms of focusing on ethical ideology and principles (placement of assets, information transparency, guarantees, and participation) and their standpoint on ethical commitment. Mzoughi et al. (2011) emphasised the effect of the ethical dimension of selling behaviour on four marketing relational variables in the banking sector (trust, satisfaction, loyalty, and commitment). The study confirmed the impact of the ethical dimension on the trust. Further, the study revealed that satisfaction had an effect on customer trust, which in turn influenced their loyalty and commitment. Kour and Khurana (2017) identified five main factors to study ethical practices in banks. The five factors identified were bank code, ethical lending, ethical orientation, professional banking, and ethical banking.

Table 2: Studies on Factors Affecting Ethics in Banks

Author	Year	Sample	Findings
Mitchell	1992		17 categories of ethical behaviour in banks were identified; most of them were internal behaviour
Božović	2007	Pristina	Application of code of ethics helps establish a defensive mechanism in the field of ethical values application
Chowdhury	2011	Bangladesh	Cost leveraging factor & value leveraging factor result in competitive advantage; high ethical practices lead to high customer satisfaction & performance

Author	Year	Sample	Findings
Icke et al.	2011	Turkey	Avoiding social exclusion & placement of assets were major factors that differentiated ethical banks & other financial institutions
Jose et al.	2011	114 European Banks	Developed an index called Radical Affinity Index (RAI) to identify & differentiate between ethical banks
Mzoughi et al.	2011	North Africa	Confirmed impact of ethical dimension on trust; satisfaction had no effect on customer trust, which in turn influenced their loyalty & commitment; selling behaviour ethics affect customer satisfaction, commitment, their trust, & loyalty
Kour & Khurana	2007	Punjab, India	Identified five factors to study ethical practices – bank code, ethical lending, ethical orientation, professional banking, & ethical banking

ETHICS IN BANKS

Icke et al. (2011) analysed the condition of ethical banking by investigating the lending mechanism of 49 Turkish banks on the basis of their ownership structures and functions. It was concluded that in terms of ownership structure, when avoiding social exclusion factors and the placement of assets was considered, state-owned banks were more ethical than private banks. They found that deposit banks were more ethical than other functional banking groups (i.e., development and participation banks) from the avoiding-exclusion aspect. Paulet (2011) studied the Swiss banking sector and emphasised that regulation was necessary, but not an adequate condition to guarantee the efficiency of financial markets, banking institutions, and the management of companies. The researcher stressed that by refocusing on their core business, banking institutions would be able to create value for the community and earn good profits. Safakali (2011) conducted a study to find out the perceived ethical quality of commercial banks from the viewpoint of small and medium enterprises in Northern Cyprus. The author grouped ethical principles into three factors, for which perceived ethical behaviours were not satisfactory. The three ethical factors were assurance, procedural justice, and sensitivity; it was found that these factors had a clarifying effect on bank satisfaction, whereas SMEs' bank satisfaction had a clarifying effect on word-of-mouth. Belás (2012) studied the Nigerian banking sector and found that there was common knowledge of the code of ethics in the banking industry; however, not all Nigerian banks fully adopted the code. The researcher inferred that the industry

was not fully sanitised to curtail it of unprofessional and unethical practices. Jasevičienė (2012) found that the codes of several banks were quite mechanical, and did not emphasise compliance with ethical norms, which resulted in an increasing number of complaints and displeasure from customers who were mainly unhappy with the conditions of lending, the rates of the services, and breakdown of the computer server while doing card transactions or e-banking operations. Further, it was found that the banks that focused on identifying and handling complaints of customers with goodwill, and in the best interests of the customer, reported fewer complaints. Belás (2013), in his study, found that the low level of loyalty and satisfaction of bank employees was transferred to the low acceptance rate of customers' need to sell the bank's products in the banking sector in Slovakia. The low level of loyalty and satisfaction also contributed to a fall in overall customer satisfaction. Mathenge (2013) conducted a study to analyse the ethical considerations in the banking industry in Kenya. The author's findings suggested that there was a need to embrace ethical values by commercial banks in creating an ethically inclined banking environment. It was concluded that commercial banks had to be at the forefront of accepting and applying ethical considerations in their banking practices, in order to create a formidable ethical banking sector in Kenya. Kour and Khurana (2017) did a comparative study of ethical practices in public and private sector banks in India. It was found that there was no difference in ethical practices between public and private sector banks in terms of bank code, professional banking, and ethical lending. However, significant differences were found in the case of ethical banking and ethical orientation of managers in both the sectors. The difference was in following rules, using fair judgment, and doing what is preached by them.

Table 3: Studies on Ethics in Banks

Author	Year	Sample	Findings
Icke et al.	2011	Turkey	State-owned banks were more ethical than private banks; deposit banks were more ethical than other functional banking groups
Paulet	2011	Swiss Banks	By altering their behaviour, banks could recover their credibility on the market & restore the confidence of the clients
Safakali	2011	Northern Cyprus	Three ethical factors – assurance, procedural justice, & sensitivity had a clarifying effect on word-of-mouth
Belás	2012	Nigeria	Banks did not follow code of ethics; banking industry not fully sanitised to curtail unprofessional & unethical practices

Author	Year	Sample	Findings
Jasevičienė	2012	Lithuania	Sample banks did not emphasise compliance with ethical norms, which resulted in larger number of complaints & displeasure from customers
Belás	2013	Slovakia	Low level of loyalty & satisfaction of bank employees led to low acceptance rate of customers' need to sell bank's product & fall in overall customer satisfaction
Methenge	2013	Kenya	There was need to embrace ethical values by commercial banks in creating an ethically inclined banking environment
Kour & Khurana	2017	Punjab, India	No difference in ethical practices between public & private sector banks in terms of bank code, professional banking, & ethical lending; significant difference in the case of ethical banking & ethical orientation of managers in both sectors; difference was in following rules, using fair judgment, & doing what is preached by them

ETHICS AND BANK FAILURES

Safakali (2005) conducted a study to explore the rationale for bank failures in Cyprus and to chalk out the professional and business ethics that was needed to provide stability in the banking and finance sector. The study stated that the factors responsible for serious ethical problems leading to financial crisis were connected lending, favouritism by the management, credits without adequate collaterals, inadequate use of funds, political interference, lack of accountability, dealing in non-financial activities, lack of transparency, illegal use of funds, and risky investments with low returns. It was concluded that ethical misconduct played a significant role in bank failures and there had been involvement of the owners, top executives, the board of directors, and the internal auditors in unethical conduct prior to such failures. Moreover, government intrusion in the central bank's independence proved to be both unethical and unfavourable to the liquidity of the banking sector.

Various studies were carried out to analyse bank failure in Nigeria. Yidawi (2005) examined a number of problems and ethical issues in the banking industry in Nigeria, which included lack of proper ethics training, dearth of qualified professional bankers, breach of Central Bank of Nigeria (CBN) and Nigeria Deposit Insurance Corporation (NDIC) guidelines, malpractices, and other frauds. The study concluded that although there was general awareness

relating to the code of ethics among the Nigerian banks, most of the banks did not implement it. Besides, increase in the number of bank forgeries and frauds compounded to the ethical problems in the Nigerian banks. Adams (2012) highlighted the failure of bank functioning in upholding the codes of ethics and professionalism. The author believed that weak banking knowledge, both in theory and practice, had resulted in disrespect of the codes of corporate governance, irresponsible diverse insider abuses by both board members and staff of banks, and ignorance of the banks of the directives of the regulators. The author further observed that systemic bank failures, and institutional and industry disorders and collapses had been the consequences of the ethical anomalies. The study recommended that the government, regulators, and the banking professionals, together, could provide a solution through necessary actions. Belás (2012), in his study, concluded that there was a general awareness of the code of ethics in the banking industry; however, not all Nigerian banks fully adopted the code. The researcher inferred that the industry was not fully sanitised to curb it of unethical and unprofessional practices. Ogbo et al. (2013), in his study, revealed that there were several unethical practices in the Nigerian banking industry. The study recommended that all stakeholders in the banking industry, the shareholders, regulators, top management, sponsors/directors, and the government, should play an active part to make sure that there was an ethical code in the banking industry in Nigeria. Adeyanju and David (2014) presented significant evidence that a majority of banks in Nigeria did not fail only due to lack of observance to ethical practices, but mostly due to other factors, such as insider abuse on lending, micro-economic instability, lending to high-risk borrowers, and deficiency in bank regulation and supervision. They recommended legal enforcement and strict sanctions to ensure mandatory adherence to ethical and professional practices in the banks.

Table 4: Studies on Ethics and Bank Failure

Author	Year	Sample	Findings (Reasons for Bank Failure)
Safakali	2005	Cyprus	Connected lending, favouritism by the management, credits without adequate collaterals, inadequate use of funds, political interference, lack of accountability, dealing in non-financial activities, lack of transparency, illegal use of funds, and risky investments with low returns
Yidawi	2005	Nigeria	Non-implementation of code of ethics despite full awareness of same

Author	Year	Sample	Findings (Reasons for Bank Failure)
Adams	2012	Nigeria	Failure of bank in upholding the codes of ethics & professionalism; disrespect of codes of corporate governance, irresponsible diverse insider abuse by both board members & staff of banks, & banks ignoring the directives of regulators
Belás	2012	Nigeria	Non-implementation of code of ethics despite full awareness of same
Ogbo et al.	2013	Nigeria	Non-implementation of code of ethics despite full awareness of same
Adeyanju & David	2014	Nigeria	Lack of observance of ethical practices, insider abuse on lending, micro-economic instability, lending to high-risk borrowers, and deficiency in bank regulation & supervision

CONCLUSION

Several research results have established that morality (in the case of customers) may be more in public banks than in private sector banks (Chatterjee & Lefcovitch 2009; Icke et al., 2011). Further, it has been observed that managers of private banks place extreme pressure on the executives, which results in an incorrect approach to clients (Belás, 2012).

Many of the above studies have confirmed that values and ethical practices in banks lead to higher customer satisfaction (Chowdhury, 2011; Mzoughi et al., 2011, Jasevičienė, 2012; Rendtorff & Mattson, 2012; Belás, 2013).

Ethical issues and ethical practices in banks have been a topic of interest in many of the above discussed studies (Goyal & Joshi, 2011; Icke et al., 2011; Jose et al., 2011; Paulet, 2011; Safakali, 2011; Senthikumar et al., 2011; Jasevičienė, 2012; Mathenge, 2013; Dorasamy et al., 2014; Fetinuic, 2014). All these studies have highlighted the importance of ethical practices on increasing customer loyalty, profitability, and productivity.

A large number of the above studies have been conducted to understand bank failure, especially in the context of Nigeria (Safakali, 2005; Yidawi, 2005; Adams, 2012; Belás, 2012; Ogbo et al., 2013; Adeyanju & David, 2014). Most of these studies pointed towards unethical practices and failure to follow the code of ethics as the main reasons for bank failure. Safakali (2005) stated that the factors responsible for serious ethical problems leading to financial crisis were connected lending, favouritism by the management, credits

without adequate collaterals, inadequate use of funds, political interference, lack of accountability, dealing in non-financial activities, illegal use of funds, lack of transparency, and risky investments with low returns.

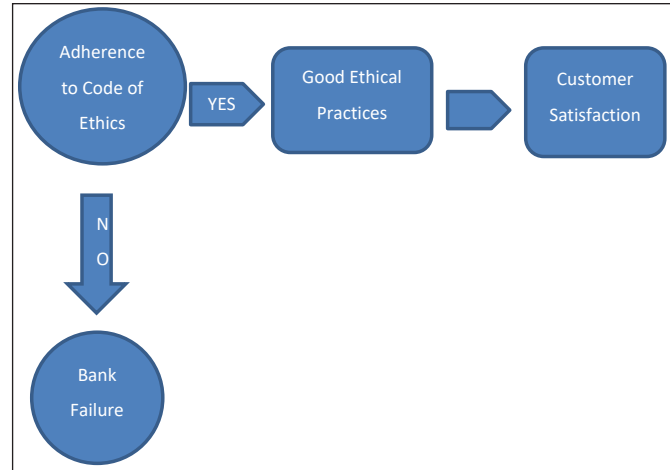


Fig. 1: Ethical Model for Banks

On the basis of the review of literature, it is found that the common thread and observation in most of the studies is that customer satisfaction in banks is related to ethical practices. Customers feel more secure and comfortable in entrusting their hard-earned money to those banks where they feel their money is safe. Unethical practices only dilute the image of the banks, leading to customer dissatisfaction, and ultimately, fewer deposits. In addition, it is found that the main reason for bank failures is non-adherence to the code of ethics. Therefore, it is suggested that for long-term profitability and higher customer satisfaction, banks should focus more on following the code of conduct, thus improving ethical practices.

Originality/Value – To the best of the author's knowledge, this is the first literature review in the area of ethics in banks. Various studies have been conducted on ethics and ethical practices in banks, but no study related to the literature review of ethics in banks was found by the author.

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