ETHICS POLICY AND RISK MITIGATION IN COMMERCIAL BANKS IN UGANDA

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Abstract

The current study set out to explore the contribution of ethics policy on risk mitigation. The study has revealed that commercial banks in Uganda have risks in areas of credit, liquidity, market, operations, compliance, taxation, and reputations. The results further revealed that ethics policy had a significant relationship with compliance [r (48) = .318, p<0.05]. Similarly compliance also significantly related to risk mitigation [r (48) =.437, p<0.01]. There was also a strong relationship between ethics policy and risk mitigation [r (48) =.380, p<0.01]. The causal effect of ethics policy on risk mitigation came out as 51%. In order to have effective risk mitigation, ethics training was proposed. A simulation should that if bank employees were given ethics training, mitigating risks in the commercial bank would improve up to 70%.

Keywords: *Ethics Policy, Risk Mitigation, Commercial Bank*

Introduction

The task of this study was to analyse the effect of ethics policy on risk mitigation in Uganda's commercial banks. The Uganda Bankers Association put in place an ethics policy commonly referred to the code of good banking practice. The cardinal aim of this policy was to ensure that risks in the commercial banks are kept at bay by promoting and maintaining high standards of professional and moral behaviour (Mutebile, 2010). The ethics policy to which most commercial banks subscribe have objectives which emphasise a number of ethical principles including those indicated here below:

Table 1: *Ethical Principles of the Bankers' Code*

Objectives	*Embedded ethics*
i) To set out the standards of good banking practice	Virtues
ii) To ensure that banks act fairly and reasonably with customers	Justice and virtue
iii) To help customers understand how their accounts operate	Virtue
iv) To promote confidence in integrity and security of banking system	Virtue
v) To maintain high standards of professional and moral behaviour in banking system	Virtue and deontology

Source: *Code of Good Banking Practice*, 2009: 2

It is noted from the Code that the ethics policy for the commercial bankers emphasise mainly three ethics principles: virtues, justice and deontology. The implication of this is that banks have to establish ethical systems and the staff have to be ethical in their dealing with customers; and when executing their professional duties as banking staff. Similarly the six fundamental principles of dealing with customers in Uganda's banking industry also emphasise virtues and justice. These principles are:

Table 2: *Ethics embedded in Fundamental Principles*

	Fundamental principles	*Embedded ethics*
a)	Avoid conflict of interest	Justice
b)	Offer service without discrimination	Justice
c)	Safeguard deposits by sound investment	Virtues
d)	Act fairly and reasonably	Justice and virtues
e)	Respect confidentiality	Virtues
f)	Ensure reliability of systems and technology	Virtues and deontology

Source: *Code of Good Banking practice*, 2009: 3

One critical issue in the Code is that it holds both the commercial banking systems and the individuals working in those banks ethically responsible.

Holding a commercial bank morally responsible is tantamount to arguing that a commercial is moral person. This implies that a commercial bank is a member of moral community of equal standing with human beings. The meaning of this is that one can legitimately ascribe moral responsibility to a commercial bank. It means that commercial banks should have privileges, rights and duties, just as it is the case with human beings. However what is not resolved is the question whether a commercial bank can have a fuller sense of responsibility in terms intentionally causing something to happen? For instance can a bank cause clients lose their money? Some ethicists like Ladd have argued that it is improper to expect organizational conduct to conform to the ordinary principles of morality. "We cannot and must not expect organizations, or their representatives acting in their official capacities, to be honest, courageous, considerate, and sympathetic or to have any kind of moral integrity. Such concepts are not in the vocabulary, so to speak, of the organizational language game" (Chryssides and Kaler, 1993). In a way this view suggests that commercial banks cannot have conscience, therefore

cannot be moral persons. So they cannot act morally on their own accord. Commercial banks that have membership with the Uganda Bankers Association (UBA) and subscribe to the ethics policy are about 27 as listed in below in table 3.

Table 3: *Commercial Banks in Uganda that are members of UBA,* 2014

	Commercial Bank	***Year opened***	***Total Assets in UGX***	***Branches***	***Member of UBA***	***Employees***
1	ABC bank Uganda	2010	30.72 bn	2	Yes	44
2	Bank of Africa Uganda	1984	446.9 bn	34	Yes	333
3	Bank of Baroda Uganda	1953	825.8 bn	15	Yes	188
4	Barclays Bank Uganda	1927	1,166 bn	44	Yes	800
5	Cairo International Bank	1995	7.5 bn	5	Yes	136
6	Centenary Bank	1983	1.45 tn	60	Yes	1,767
7	Citibank Uganda	1999	587.4 bn	1	Yes	40
8	Commercial Bank of Africa	2014	45.4 bn	1	Yes	35
9	Crane Bank	1995	1.45 tn	38	Yes	500
10	Diamond Trust Bank	1945	628.5 bn	26	Yes	1,264
11	DFCU bank	1964	1.197 tn	36	Yes	476
12	Eco Bank Uganda	2009	164.4 bn	11	Yes	145
13	Equity Bank Uganda	2008	370 bn	39	Yes	550
14	GT Bank Uganda	2008	89.8bn	7	Yes	120
15	Global Trust Bank	2008	90 bn	26	Yes	200
16	Housing Finance Bank	1967	558.4 bn	17	Yes	300
17	KCB Bank Uganda	2007	335.5 bn	16	Yes	336
18	NC Bank Uganda	2012	34 bn	1	Yes	36
19	Orient Bank	1993	517.7bn	20	Yes	400
20	Stanbic Bank Uganda	1906	3.24 tn	93	Yes	1,859
21	Standard Chartered Bank	1912	2.5 tn	14	Yes	629
22	Tropical Bank	1973	215 bn	14	Yes	412
23	Uganda Development bank	1972	146.9bn	1	Yes	36
24	United Bank of Africa	2008	29 bn	10	Yes	150
25	Imperial Bank Uganda	2011	214.65 bn	5	Yes	100
26	Bank of India	2012	896 mn	1	Yes	36
27	Finance Trust Bank Uganda	1984	92.3 bn	33	Yes	312

On the other hand commercial banks like other companies can be regarded to have a conscience and the language of ethics does apply to them. This is possible because the moral responsibility of persons can be projected to commercial banks. Moral responsibility is based on three things:

(a) Someone to blame – the casual sense
(b) Something has to be done – the duty
(c) Some trustworthiness can be expected – the credibility

The causal sense can be applied to legal and moral contexts in that the cause of actions and events can be traced. So responsibility here has to do with finding out who is answerable in a given situation. The aim is to determine someone's intention, free will, degree of participation, and appropriate reward or punishment. Since commercial banks can be rewarded or punished, it means they are moral persons. For that matter they can be held morally responsible. In view of the foregoing discussion, it is right to infer that the ethics policy as introduced by the Uganda Bankers Association, applies to both the banks as institutions and to the individuals who work and make decisions in those banks. It is also intended that if the banks followed the ethics policy tenaciously there would be negligible risks especially those arising out of unethical decisions.

Problem statement

The problem being examined in this study is that although there is an ethics policy which the Uganda Bankers Association put in place to regulate the moral actions banks and thereby mitigate risks, there have been worries and fears about risks in the Ugandan commercial banks which have been deemed to be just increasing. The risks include the following:

(1) *Credit risk* – Acting unprofessionally and negligently led risk. For instance there are cases of customers who acquired loans and were supposed to pay interest on the loans. However, it turned out that interest was not loaded for some loans. In Bank *AAA* the loan of UGX4,500,000 and in Bank *BBB* the loan of UGX12,630,500 were loaded without interest. In some other banks (*EEE*, *III* and *LLL*) accounts were overdrawn without authorisation by the credit departments. Some of the amount discovered in bank *BBB* was UGX 22,742,200; in bank *DDD* was UGX8,860,900; and in Bank *KKK* UGX8,000,300. Some closed accounts were also overdrawn by close to UGX500,000 in Bank *CCC*. One of the risks involved in all these

incidents was loss. The overdrawn accounts put the bank at risk and management would easily overstate income. Furthermore, charges for replaced ATM cards were never recovered thereby creating loss.

(2) *Liquidity risk* - There were daily calls on cash resources from overnight deposits, current accounts, maturing deposits and calls on cash settled contingencies which the bank could not meet because of lack of resources. In 2010, some banks had a liquidity gap of as much as UGX 573,352,000. In 2011 there were approximately 20 payments totalling UGX16,056,500 made by tellers when the vouchers had irregularities like inconsistency in figures and words, no officer's signature, no domicile, no title account, and no stamp of the bank. All this exposed banks to the risk of financial loss on the part of banks (*Risk Assurance Report*, 2010, 2011 and 2012).

(3) *Risk of credit quality* - Bank of Uganda 2012 supervision found a "rising risk from deterioration in loan quality. These risks materialised in2013 and reduced bank profitability. By December 2013, systematic risk increased, driven by continued rise in bad loans. Non-performing loans rose to their highest level of 5.6% since 2004 (*BOU supervision report*, 2013).

(4) *Risk of managing financial institutions* – It is intimated that risk management in financial institutions in Uganda gained prominence in the late 1990s when commercial banks exhibited deep seated failures in this perspective (Bagyenda, 2011).

All these risks occur in spite of the existence of the ethics policy which is intended to mitigate risks. It therefore raises the question of how far does ethics policy go in mitigating risk in commercial banks in Uganda.

Purpose of the Study

The study analyses the contribution of ethics policy to mitigating risks in commercial banks in Uganda.

Specific Objective

1. To analyse the relationship between ethics policy and compliance with legal requirements
2. To assess the contribution of compliance with legal requirements to risk mitigation in Ugandan commercial banks.
3. To determine the contribution of the ethic policy to risk mitigation in Ugandan banks.

Hypothesis

The hypothesis which was generated for the current study was coterminous with the objective of the study.

Ethics Policy relates to Compliance

H_0^1 Ethics policy does not significantly relate to compliance with legal requirements

H_A^1 Ethics policy significantly relates to compliance with legal requirements

Compliance and Risk Mitigation

H_0^2 Compliance with legal requirements has no significant contribution to risk mitigation in Ugandan commercial banks

H_A^2 Compliance with legal requirements has a significant contribution to risk mitigation in Ugandan commercial banks

Ethics Policy mitigates risks in Commercial Banks in Uganda

H_0^1 There is no significant contribution of the ethics policy to mitigation of risks in Ugandan commercial banks.

H_A^1 There is a significant contribution of the ethics policy to mitigation of risks in Ugandan commercial banks.

Literature Review

Ethics Policy

The term ethics policy can be examined looking at each word separately. The word ethics is from Greek *Ἠθικά* that is *Ethika* meaning decisions or actions that are valued. The decisions or actions came into ethics discourse if they affect a person positively or negatively.

Ethics in Risk Management Practices

A study seeking to explore Ethics in risk management practices was conducted by Caldarelli, Fiondella, Maffei, Spano and Zagaria (2012). They advanced the view that ethics in risk management is the new driving value for business activities. Whereas this study is important, it does not address the same issues as those raised by the current study. It is proposed by several authors that it is possible to manage risk ethically (Robins and Fleming, 2004). In another study Mande (2012) explores the contribution of ethics training to MBA students' readiness to manage ethically. These studies are useful and helpful but they do not explore how much ethics

policy mitigates the risks commercial banks in Uganda face. This gap is what the current study tries to investigate and probably fill.

Ethics as a Risk Management Strategy

There work of Francis and Armstrong (2014) contended that ethics was a risk management strategy. With this kind of strategy it is possible to identify potential problems, prevent fraud, preserve corporate reputation, and mitigate court penalties. Although this study is good, it is worth noting that its orientation is Australian which makes it generalise and apply to Ugandan context. This is already a gap that the current study seek to fill. In another study it has been argued that ethics acts as a strategic enabler for any organisation's success and sustainability. It can also serve as a builder by giving an organisation a powerful sense of identity, instilling confidence in its staff and evoking security in stakeholders. It is further observed that ethics is an equally important defensive strategy. Ethics policy can help to identify the issues before they compound into problems. Ethics can prevent outright fraudulent behaviour and preserve reputation and brand (Campbell, 2009).

Ethics of Risk Management

The link between ethics and risk management has already been established (Young, 2004). The paper by Boatright (2014) indicates that there are four key highlights. These are: (1) determining the risks to be managed, by whom and for whose benefit; (2) maintaining of competent control; (3) top management understanding the risks and potential gains; and (4) quantifying the probability of extremely rare events. These are critical highlights except that they are not enough to explain the risk issues in Ugandan commercial banks. This leaves a gap for the current study.

Risk

A lot has been said about risks in general. However in the commercial banking sector risk can be considered as a fundamental element that drives financial behaviour. Risk is omnipresent in every financial system in the real world (Arunkumar, 2005). The current study agrees with the above submission. This is because it is now common knowledge in the finance world that the success and survival of the banking institutions depend largely on effective management of risk. Commercial banks devise many ways to deal with risk. One such a way to deal with risk is implementation of ethics policy. In the Wharton studies, types of risk especially credit risk, counterparty risk, liquidity risk, legal risk, foreign exchange risk, and interest risk are recommended to be studied (Santamero, 1997). The current

study seeks to analyse how ethics policy has mitigated the effects of such types of risk in Ugandan commercial banks.

Compliance

Compliance is quite important. Compliance officers play a key role of assessing risks in areas of investment, market, credit, operations, funding and liquidity (di Florio, 2011). This observation is one of the points the current study seeks to conform and also gauge as far ethics policy is concerned in Uganda's commercial banks.

Methodology

Research design

The research design adopted for this study was the cross sectional survey (Amin, 2005). This study was designed to use various methods to obtain data and other facts. Mixed methods research is defined as a "research in which the investigator collects and analyses data, integrates the findings, and draws inferences using both qualitative and quantitative approaches and methods in a single study" (Creswell *et al* 2005). The term cross-sectional research is sometimes used to describe the same phenomenon of applying many research methods. It is a triangulation approach that was used. The term triangulation refers to a "combination of methodologies in a study of the same phenomenon" (Gill and Johnson 1991:50; White, 2002: 26).

Triangulation has a number of benefits. One, multiple and independent methods help the study to attain greater validity and reliability than a single methodological approach. Two, it allows quantitative and qualitative methodologies to be used for the same study. Three, it cuts out the limitations a specific methodology would impose on the study. So the use of triangulation enabled the current study to harvest all the above mentioned benefits. Several other research activities like administration of questionnaire, reviewing literature and interviewing some bank officials were carried out simultaneously.

Sampling technique

The minimum sample for the study was determined using Roscoe's (1975) rule of the thumb approach. Roscoe contended that in social science research, any number of respondents between 30 and 500 is sufficient to give credible results. So the figure of 48 as minimum sample was determined using Roscoe's rule of the thumb. This number was deemed to be sufficient to yield results that reflect what views and experiences of

commercial banks in Uganda. After determining the number of respondents, purposive sampling was applied to select the respondents to the questionnaire. This is a judgmental sampling technique whereby samples are sampled on the presumption that they would satisfy the research objectives (White, 2002). There was a deliberate purpose of focusing on only those who work in accounts and auditing.

Regarding which individuals had to respond to the questionnaire, convenience sampling was employed. Convenience sampling refers to the collection of information from members of the financial department who were conveniently available to provide it (Sekaran, 2003: 276). So employees in four departments of auditing, credit, risk and compliance were requested to respond to the questionnaire. In addition to that twelve branch managers were interviewed. The unit of analysis was therefore the managers and employees in departments that deal with risk more regularly.

Table 4: Respondents according to departments

	Bank	Auditing	Credit	Risk	Compliance	Total
1	AAA	1	1	1	1	4
2	BBB	1	1	1	1	4
3	CCC	1	1	1	1	4
4	DDD	1	1	1	1	4
5	EEE	1	1	1	1	4
6	FFF	1	1	1	1	4
7	GGG	1	1	1	1	4
8	HHH	1	1	1	1	4
9	III	1	1	1	1	4
10	JJJ	1	1	1	1	4
11	KKK	1	1	1	1	4
12	LLL	1	1	1	1	4
	Total	12	12	12	12	48

Source *Field data*

In order to maintain confidentiality, the names of the participating banks were assigned alphabetical names AAA through LLL.

Data collection methods

The methods used to collect information and data included the following.

(*a*) *Unstructured interview method*

Unstructured interview is one of the four types of interview. Others being; the structured, the non-directive, and the focused (Cohen and Manion, 1994: 273). The unstructured interviewing is where there is great freedom and flexibility (Saunders, *et al*, 1997). This method was deemed to be appropriate for branch managers of the twelve selected commercial banks in Kampala.

(b) Survey method

This is the method of data collection by which the respondents provide answers in a pre-determined order (Saunders, 1997: 243). For this study, a questionnaire of 52 items was administered to 48 bank employees. The items on the questionnaire covered a number three broad areas; ethics, compliance, credit and risk. A survey method in some instances is quite useful (Gilbert, 1995: 95). It is possible to get the questionnaire to many people (48) at the same time. Through the administration of the questionnaire, this study was able to acquire information, opinions, and experiences.

(c) Review of primary records

It was possible to review some of the records especially the annual reports of the respective banks. Some reports had already been uploaded on their websites. The main items reviewed were data to do with issues of risk in the areas of credit and compliance.

(d) Review of secondary literature

Secondary literature was manly the published books and articles. These were read so as to clarify the issues in the areas of ethics policy, risks in the banking sector, credit and compliance with legal and policy requirements. The library of Nkumba university were accessed.. Some internet materials especially databases that the university subscribe to were retrieved and studied for a period of two months.

Validity and Reliability

The issue of validity and reliability were taken into account. White (2002) pointed out that validity is concerned with the idea that the research design fully addresses the research objectives that have to be achieved. In the current study, validity was established through a validity test using the Content Validity Index (CVI). The product of the CVI test was 0.772. Since

conventional research wisdom requires that a good research be ≥ 0.6 (either equal or greater than 60%), it meant that the questions posed were relevant and valid to the study variables.

Reliability is important because the data collection instrument must have the ability to consistently yield the same results when repeated measurements are taken of the same individuals under the same conditions (Koul, 2004: 130). The reliability was done using the Cronbach's (1964) alpha (α) test in order to ascertain the internal consistency of the study variables. The results of the reliability test were shown in the table below:

Table 5: *Reliability.*

	Variables	Cronbach Alpha Coefficients
1	Ethics policy	0.791
2	Compliance	0.833
3	Risk	0.767
4	Credit	0.801
	Average	**0.775**

Source: *Computed using SPSS*

The average coefficient is 0.775 whose implication is that the study variables were reliable and consistent. The average of 77% is above the usual 60% which is considered to be cut off point.

Data analysis

The quantitative data generated during the field research was collated and analysed using the SPSS software program. Correlations and regressions were done in order to effect of independent variable on intervening and dependent variables. These were applied so as to accurately determine the relationships between ethics policy and risk mitigation in banks.

Similarly the qualitative data was analysed by use of various approaches. Some data from literature reviewed critically in order to clarify concepts. Some information was assessed so as to determine its applicability to the current study. Furthermore past studies were carefully studied so as to identify the gaps that the current study had to fill.

Findings and Discussion on Uganda Commercial Banks

The concept of Risk

There is no universal held definition of risk. Sometimes the meaning of word "risk" varies depending on context. For instance it is commonly used

in insurance to refer to insured items like cars, buildings and others. Risk has also been defined as: a combination of hazards measured by probability; a condition in which losses are possible. From this we define risk to mean the variation of actual outcomes from expected outcomes. For instance, in an investment decision - expected outcome = profit; if actual outcome = loss, then risk (Skelton, 1997).

Many times risks can be classified into several categories depending on context. For instance there are: (a) Inherent risks; (b) Unsystematic risks; (c) Incidental risks; (d) Event risks also known as pure risks arise from natural phenomena mainly and human error;(e) Fundamental risks are impersonal in origin and affect society at large e.g. war, drought; (f) Particular risks are personal in origin and affect individuals or small groups e.g. fire, theft, vehicle accidents and the like. The current study is concerned with the so-called incidental risks especially credit risk, interest rate risk, liquidity risk, investment risk, and currency risks.

Risks faced by commercial banks in Uganda

There are seven types of risks that are significant and common to commercial banks in Uganda.

Table 6*: Responses on whether a bank has ever worries of risk*

	Bank	*Credit*	*Taxation*	*Compliance*	*Liquidity*	*Market*	*Operations*	*Reputation*
1	AAA	✓	✓	✓	✓	✓	✓	✓
2	BBB	✓	✓	✓	✓	✓	✓	✓
3	CCC	✓	✓	✓	✓	✓	✓	✓
4	DDD	✓	✓	✓	✓	✓	✓	✓
5	EEE	✓	✓	✓	✓	✓	✓	✓
6	FFF	✓	✓	✓	✓	✓	✓	✓
7	GGG	✓	✓	✓	✓	✓	✓	✓
8	HHH	✓	✓	✓	✓	✓	✓	✓
9	III	✓	✓	✓	✓	✓	✓	✓
10	JJJ	✓	✓	✓	✓	✓	✓	✓
11	KKK	✓	✓	✓	✓	✓	✓	✓
12	LLL	✓	✓	✓	✓	✓	✓	✓

Source: *Field Research*

The table above indicate the responses of bank employees to the question whether the commercial bank has ever had of incidents of risk in each of the seven areas. It emerged clearly that all the participating banks have had incidents of risk in the last five years that is between 2010 and 2014. Bad ethics or failure to adhere to the ethical principles had had a disastrous effect on banks. The commercial banks in Uganda that failed due to unethical performance are:

Table 7: *Banks that were closed in Uganda*

	Closed	*Remarks*
1	Greenland Bank	The closure of these commercial banks was caused by unethical activities. The activities were linked to liquidity risks, compliance risks, credit risks and operational risks.
2	Uganda Commercial Bank	
3	Fina Bank	
4	National Bank of Commerce	
5	Nile Bank	
6	Global Trustee Bank	
7	Co-operative Bank	
8	International Credit Bank	

The failure of the above banks was ascribed to "unethical practices". The situation was referred to as one of poor and abusive management which exposed the bank to the seven described risks consequently the bank had to be closed (Mwesigwa, 2014). It has also been observed that profitability of banks has been declining while non-performing assets and loans have been on upward trend (Businge, 2014).

For clarity purposes the types of risks experienced by the commercial banks in Uganda are explained here below one by one.

(1) Credit Risk

Risk is a big concern for all financial institutions. So a bank has to set in place comprehensive resources, expertise and controls to ensure efficient and effective management of credit risk. In lending transactions; credit risk arises through non-performance by counterparty for credit facilities utilized. These facilities are typically loans and advances, including the advancement of securities and contracts to support customer obligations (such as letters of credit and guarantees).In trading activities; credit risk arises due to non-performance by a counterparty for payments linked to trading related financial obligations.

In Uganda banks, bad debts are considered to be an almost permanent fixture on their balance sheets. The loans written off by the banks have massively increased. For instance Centenary Bank wrote off UGX7.8bn of bad loans, up from UGX4bn in 2012. DFCU Bank wrote off UGX 15bn, nearly twice as much as the UGX8.7bn of 2012. Standard Chartered Bank's non-performing loans and other assets increased from UGX10bn in 2012 to UGX120bn in 2013 (Mwesigwa, 2014). Non-performing loans are a sum of borrowed money upon which the debtor has not made his or her scheduled payments. Bad debts cannot be blamed on bad ethics alone but also on slow economic activity that contributed to more bad commercial loans."The level of non-performing loans has increased from 4.9 per cent in September to 6.9 per cent in December 2013. The credit risk was partly caused by unethical actions both locally and internationally.

(2) Liquidity Risk

Liquidity risk arises if the bank has insufficient funds or marketable assets available to fulfil their current or future cash flow obligations at the least possible cost. The nature of banking and trading activities results in a continuous exposure to liquidity risk. The bank's liquidity risk management framework however is designed to measure and manage the liquidity position at various levels to ensure that all payment obligations can be met under both normal and stressed conditions. Liquidity risk is one of the risks commercial banks assume. This is one of the challenges for the Ugandan banks (Donat and Asa, 2012). Commercial banks have had liquidity risks. When one bank was assessed, it was rated to be in marginal ranking. This meant that that bank had put UGX36billion depositors' cash at risk. The same bank was involved in a controversy whereby it was said that it had paid out UGX63 billion to 1018 non-existent "ghost" pensioners. Payments were done in a suspicious (unethical) manner (Obore, 2013).

(3) Market risk

Market risk arises from a decrease in the market value of a portfolio of financial instruments caused by an adverse move in market variables such as equity, bond and commodity prices, currency exchange rates, interest rates and credit spreads, and implied volatilities on all of the above. Market risk exposures as a result of trading activities are contained within the bank's corporate and investment banking trading operations. The bank manages market risk through a range of market risk and capital risk limits.

Banking-related market risk exposure principally involves the management of the potential adverse effect of interest rate movements on

net interest income and the economic value of equity. This structural interest rate risk is caused by the differing re-pricing characteristics of banking assets and liabilities. The governance framework adopted for the management of structural interest rate risk mirrors that of liquidity risk management in terms of committee structures and the setting of standards, policies and limits. This is also true for the monitoring process and internal controls.

(4) ***Operational Risk***

Operational risk is the risk of loss suffered as a result of inadequacy of, or a failure in internal processes, people, systems or external events. The bank recognizes the significance of operational risk, which is inherent in all areas of our business. The bank's operational risk governance standard codifies the core governing principles for operational risk management and defines a common framework with the basic components for the identification, assessment, management, monitoring and reporting of operational risk. This common framework defines the minimum requirements whilst ensuring an element of flexibility for each business unit's particular operating environments. This framework is further supported by a set of comprehensive operational risk management policies.

The bank's approach to managing operational risk is to adopt practices that are fit for the purpose to increase the efficiency and effectiveness of the bank's resources, minimize losses and effectively utilize opportunities. This approach is aligned to the bank's enterprise risk management framework and adopts the sound practices recommended by various sources, including the Basel II Accord's Sound Practices for the Management and Supervision of Operational Risk. The independent operational risk functions perform control and oversight roles, including the setting of appropriate policies, governance standards and tools. The tools include:

(a) A centralized operational loss database providing management reports used to identify improvements to processes and controls arising from loss trends;
(b) Risk and control self assessment through which existing and potential future risks and their related controls are identified and assessed; and
(c) Key risk indicators which measure specific factors to provide an early warning to proactively address potential exposures.

The bank further maintains a comprehensive insurance programme to cover losses from fraud, theft, professional liability claims and damage to

physical assets and operates a comprehensive internal audit programme on the entire Bank's operations. Resource to support fraud prevention has been enhanced and the implementation and continual review of the adequacy of the monitoring and control processes on all bank transactions has also been set as a focus area. The bank has in addition, set up a structure for a forensic services unit, which is mandated by the audit committee, and is responsible for the application of a prudent fraud risk management practice throughout the bank. The strategic approach focuses on fraud prevention, detection, investigation and whistle blowing activities. The bank maintains a zero tolerance approach towards fraud and dishonesty.

(5) Compliance Risk

Compliance is an independent core risk management activity, which also has unrestricted access to the managing director and the chairman of the board. The bank is subject to extensive supervisory and regulatory regimes, and while the executive management remains responsible for overseeing the management of the bank's compliance risk, group compliance actively engages with management and the compliance officers within subsidiaries to proactively support the generation of legal, ethical and profitable business. The bank operates a centralized compliance risk management structure run by a fully equipped specialized unit that grants oversight on all compliance related matters. The Compliance unit provides leadership and guidance on compliance with money laundering, terrorist financing, occupational health and safety and emerging legislative developments. The regulatory services unit provides training and awareness on regulatory developments, particularly in the area of consumer protection.

(6) Taxation Risk

Taxation risk is the possibility of suffering loss, financial or otherwise, as a result of the misapplication of tax systems (whether in legislative systems, rulings or practices) applicable to the entire spectrum of taxes and other fiscal imposts to which the bank is subject. The bank fulfils its responsibilities under tax law in relation to compliance, planning or client service matters. Tax law includes all responsibilities which the bank may have in relation to company taxes, personal taxes, capital gains taxes, indirect taxes and tax administration. The identification and management of tax risk is the primary objective of the bank tax and regulatory function, and this objective is achieved through the application of a tax risk matrix

approach, which measures the fulfilment of tax responsibilities against the specific requirements of each category of tax to which the bank is exposed, in the context of the various types of activity the bank conducts.

(7) Reputational risk.

The safeguarding of the bank's reputation is of paramount importance to its continued operations and is the responsibility of every member of staff. Reputational risks can arise from social, ethical or environmental issues, or as a consequence of operational risk events. Management of all operating activities is required to establish a strong internal control structure to minimize the risk of operational and financial failure and to ensure that a full assessment of reputational implications is made before strategic decisions are taken. The bank sets clear standards and policies on all major aspects of business and these standards and policies are integral to the bank's system of internal control and are communicated though procedures, manuals and appropriate staff training. Reputational risks are considered and assessed by the board, the bank risk management committee, the bank audit committee and executive management**.** For that reason therefore, the current study constructed a hypothesis to test whether the adoption of the above code of conduct contributed significantly to the enhancement of risk management in the commercial banks in Uganda.

Results of the Tests of the Hypotheses

The ethics policy for commercial banks in Uganda was also assessed for its compliance with the legal and regulatory requirements imposed on the financial institutions in the country. For instance the Bank of Uganda, in its capacity as the central bank of the nations has supervisory roles that carries out on all financial institutions all categories. So, a hypothesis was developed to test the compliance with their own accounting procedures with legal and regulatory requirements. Hypothesis was tested as indicated in the results below.

Test of hypothesis 1 (H_0^1): Ethics Policy and *Compliance*

The first null hypothesis (H_0^1) read "There is no significant relationship ethics policy and compliance". The relationship between ethics policy and legal requirements was first determined through a bivariate correlation. The results indicated that there was a negative significant relationship between ethics policy and compliance(r (48) =.318, P<0.05). The hypothesis was further tested using a simple linear regression. The results revealed that there was a linear relationship between ethics policy and compliance with legal requirements (F (1,46) =5.168, P<0.05). As can be noted from this

statistic, having proper ethics policy in place go hand in hand with compliance with legal and regulatory requirements. It was also found that the Adj. $R^2$was .081 which when calculated meant that ethics policy contributed 8% to making compliance with legal requirement less difficult.

***Table 8:** Ethics policy and compliance*

Model	Unstandardised Coefficients		Standardised coefficients	t	Sig.
	B	Std Error	Beta		
Constant	6.095	.782		7.789	.000
Legal requirements	.410	.181	.318	2.273	.028

a. dependent variable: ethics policy

The results of Beta =.318, P<0.05 as given table 4:3 above clearly show that there was a low negative significant relationship between having in place accounting procedures and compliance with legal and regulatory requirements of the banking institutions in the country. It meant that the more effective the accounting procedures are, the less difficult it becomes to implement the legal requirements. Given the above results, one can conclude that the null hypothesis was rejected and the alternate hypothesis (H_A^1) which stated that, "There is a significant relationship ethics policy and compliance with the legal and regulatory standards" was supported instead.

Test of Hypothesis 2 (H_0^2): Compliance and Risk Mitigation

The test of hypothesis 2 on compliance and risk mitigation was done first the bivariate correlation. This yielded results (r (48) =.437, P<0.01) which indicated that the more the above compliance with legal and other regulatory requirements the more risks are mitigated. So compliance is an effective technique in mitigating the risks and their effects. A simple linear regression was also carried out to confirm the contribution of compliance to effectively mitigating risks in the commercial banks. First, a linear relationship (F (1,46) =10.849, P<0.01) revealed that the more the compliance the more the risk mitigation. Second, an Adj. R^2 was .173 which meant that compliance alone contributed 17% to the effectiveness in mitigating risks. The coefficients of the regression are shown in table 4:1 below:

Table 9: *Compliance and Risk Mitigation*

Model	Unstandardised Coefficients		Standardised coefficients	t	Sig.
	B	Std Error	Beta		
Constant	1.130	1.710		.660	.000
Compliance with legal requirements	1.260	.382	.437	3.294	.002

a. dependent variable: Risk mitigation

Table 4:1 above gives the results as Beta =.437, P<0.01. This points the fact that the compliance alone had a moderate positive significant contribution to risk mitigation in commercial banks. The results therefore proved that the compliance and risk mitigation execute its risk management activities bring about effectiveness.

Test of Hypothesis 3(H_0^3): Contribution of Ethics Policy to Risk Mitigation

H_0^3: There is no significant contribution of ethics policy to risk mitigation. The above hypothesis was test first using a bivariate correlation which yielded the following results: r (48) =.380, P<0.01. It revealed therefore that there was a positive significant relationship between ethics policy and risk mitigation in commercial banks of Uganda.

The hypothesis was also subjected to a linear regression matrix in order to determine how much ethics policy contributed to risk mitigation. The regression test produced results as shown in the table below:

Table 10: *The Contribution of Ethics Policy to Risk Mitigation*

Model	Unstandardised Coefficients		Standardised coefficients	t	Sig.
	B	Std Error	Beta		
Constant	7.525	.303		24.862	.000
Ethics policy	.675	.067	.380	10.106	.000

a. dependent variable: Risk Mitigation

The model summary of the regression test produced an Adj. R^2 of .689 which meant that the adoption of the code of conduct contributed 69% to the enhancement of risk mitigation activities. The remaining 31% was contributed by other factors outside the scope of the current study. There was also a linear relationship between ethics policy and risk mitigation (F (1, 46) =102,139, P<0.01). From this statistic, it is possible to conclude that the more commercial bank staff adopt the ethics policy, the better the mitigation of risks in the banks. Furthermore, the results of the regression

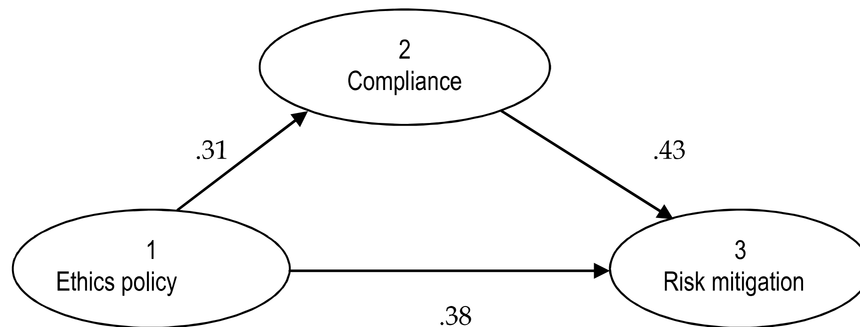
(Beta = .380, P<0.01) indicated that the ethics policy is a strong contributor to mitigation of risks. In the light of the above results, it is suitable to state that the null hypothesis *H* that "there is no significant contribution of ethics policy on risk mitigation in commercial banks" was rejected. The alternate hypothesis H_A^3 stated that "there is a there is a significant contribution of ethics policy to risk mitigation in commercial banks" was upheld.

HYPOTHETICAL MODEL FOR ETHICS POLICY AND RISK MITIGATION

The hypothetical model was used to determine the overall effect of ethics policy on risk mitigation. The hypothetical model therefore provides a reliable explanation that risk mitigation is a function of ethics policy, that is, RM = f (EP). In the explanation the following are taken into account:

(a) Determining variables – in the model there is an independent variable (ethics policy), and moderating variable (compliance), and a dependent variable (risk mitigation).
(b) Establishing causal paths – the causal paths relevant to variable (3) which is risk mitigation are paths from (1) to (2) to (3); and from (1) to (3).
(c) Stating assumptions – e.g. all relations are linear,
(d) Variables are measured linearly left to right.

The paths for the hypothesised empirical model



The paths in the hypothesised model above establish the following relationships:

(1) A positive significant relationship between ethics policy and compliance
(2) A positive significant relationship between compliance and risk mitigation
(3) A positive significant relationship between ethics policy and risk mitigation

The results were as the paths coefficients indicate:

Paths	Variable	coefficients
P21	= Ethics policy and compliance	.31
P32	= Compliance and risk mitigation	.43
P31	= Ethics policy and risk mitigation	.38

Variable 1 (ethics policy) is the only exogenous variable because it has no arrows pointing to it. This leaves two endogenous variables in the model, that is variable 2 (compliance) and variable 3 (risk mitigation). Each of these variables is explained by one or two variables.

Effects of decomposition

The paths coefficients were used to decompose correlations in the model into direct and indirect effects corresponding to direct and indirect paths reflected in the arrows of the model. This is based on rule that in a linear system the total causal effect of variable A on variable B is the sum of the values of all the paths from A to B. Risk mitigation is the dependent variable while ethics policy is the independent variable, the indirect effects and calculated by multiplying the paths coefficients for each path from ethics policy to risk mitigation

= ethics policy ⟶ compliance risk ⟶ mitigation

= .31 x .43 = .1333 ≅ .13

So, .13 is the total indirect effect of ethics policy on risk mitigation, plus the direct effect of .38. The total causal effect of ethics policy on risk mitigation is (.13+.38) .51. In view of the above model, it is appropriate to infer that ethics policy is a major determinant of the risk mitigation. The other factors which account for the remaining .49 should be only peripheral in the matters of risk mitigation in a workplace.

Although the total causal effect of 51% is moderate, there is some discontent about the risks in Ugandan commercial banks (BOU annual reports of 2011, 2012 and 2013).

Recommendation: Ethics Training For Bank Employees

As already indicated, ethics policy alone contributes 51% to risk mitigation in the commercial banks. In order to boost the contribution of ethics to risk mitigation, there should intensive training in ethics for all employees in the banking industry in Uganda.

Simulating the contribution of training in ethics

How much the training in ethics can contribute to risk mitigation, can be determined by carrying out a simulation. The simulation is carried out in following steps:

Step 1 the percentage of total causal effect is subtracted from 100%. In this study, the total causal effect from the hypothetical model is 51%. So 100% minus 51% leaves 49%.

Step 2 the product in step 1 above is multiplied by the direct effect. In the current study, this is .51 x .38 = .19. So the contribution of training in ethics is 19%.

Step 3 The product in step 2 is added to the total causal effect in order to derive the total causal effect after simulation. In this study the 19% is added to the 51% giving a final figure of 70%.

Step 4 Conclusion based on the simulation is that it is viable to adopt the training of bank employees in ethics because it promises to add value (19%) to the risk mitigation.

Summary of the Chapter

It short it can be stated that this paper set out to present facts about ethics policy and risk mitigation in commercial banks in Uganda. The concepts of ethics policy, compliance and risk plus risk mitigation have been defined. It was found that ethics policy alone contributes 51% to risk mitigation in the commercial banks. It is proposed that if ethics training is adopted, the contribution of ethics to risk mitigation would rise to 70% from the initial 51%.

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