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# Corporate Regulation of Unethical Practices: Assessment of Nigeria's Commercial Banking Industry

Olabode A. Oyewunmi<sup>1\*</sup>, Olamide Olusanmi<sup>2</sup>, Olusola J. Olujobi<sup>3</sup>, Folashade Adegboye<sup>4</sup>

<sup>1</sup>College of Business and Social Sciences, Covenant University, Ogun State, Nigeria, <sup>2</sup>College of Business and Social Sciences, Covenant University, Ogun State, Nigeria, <sup>3</sup>College of Business and Social Sciences, Covenant University, Ogun State, Nigeria, <sup>4</sup>College of Business and Social Sciences, Covenant University, Ogun State, Nigeria.

\*Email: [olabode.oyewunmi@covenantuniversity.edu.ng](mailto:olabode.oyewunmi@covenantuniversity.edu.ng)

## ABSTRACT

Evidently, a culture of due compliance has been eroded on multiple levels within Nigeria's commercial banking industry. Hence, corporate values and professional ethics are being sacrificed on the grounds of; being competitive, returning impressive profit margins and increasing market share. Historical antecedents and emerging trends indicate the long term adverse effects of corporate malpractices, especially when left unmitigated by affected stakeholders. The appreciable decline in global oil prices has reenergized corporate regulatory oversight in Nigeria. The aim in this regard and as widely publicized; is to sanitize the wider business environment and importantly renew the public trust, domestically and internationally. Apparent trends of insider dealing practices subsist in Nigeria's banking industry, even though very limited conclusive cases are available for exhaustive analysis. This fact is further validated by the various interventions of the requisite regulatory agencies, coupled with the local and international commentaries in this regards. Instructively, deployment of statutory-oversight by the requisite agencies has prevented a systemic collapse of banking industry. The paper also succinctly explored the essence of the stakeholder theory, as a basis to validate the necessity of corporate regulatory intervention. Relevant evidences, specific statutes and others verifiable sources utilized to expound on the theme of the paper. It is opined that there must be active collaborations between corporate stakeholders and the regulatory structures, particularly against the backdrop of Nigeria's unfolding socio-economic peculiarities.

**Keywords:** Regulation, Banking, Compliance, Unethical, Insider Dealing and Stakeholder

**JEL Classifications:** E52, E58

## 1. INTRODUCTION

The significance of the relationship between corporate regulation and unethical practices, notably insider dealings, cannot be relegated, especially when considered in the context of a transitional banking industry. Such an assessment becomes more meaningful when construed in the light of some happenings associated with Nigeria's commercial banking industry. Moreover, the adoption of various technological platforms, coupled with increased access and market penetration further affirms the need for elevating the monitoring of banking transactions. Such an approach will contribute in measurable respects to promoting the corporate values, professional ethics as well as the overall sanctity of the industry.

Trends of insider dealings related to the Nigerian banking industry system have historical antecedents dating back over three decades.

The Central Bank of Nigeria (CBN) examiners identified that a wide range of corporate abuses and unethical practices were significantly impairing corporate performance in the commercial banking industry. Instructively, the principal factor underlying bank failure in as regards 1980s and 1990s has been attributed to board and management related practices consequently, in the early to the mid-2000s, there was a recapitalization policy drive, which manifested in several public shares offers as well as mergers and acquisitions. It is also instructive to note the changes in the top hierarchy of the Apex Bank and its related policy shifts and adjustments.

It is very evident that poor corporate governance practices have manifested in deficiencies relative to; banks earning assets especially loans, maintenance of the statutory obligor limit and advances connected with insider abuse. Such can also be attributed

to management inefficiencies and as well as the escalation of insider transactions. A more robust implementation in 2015 of treasury single account has further brought to the light the scope of unhealthy practices amongst several commercial banks. It particularly highlighted unethical practice of holding multiple accounts by individuals and corporate bodies which facilitated round tripping of funds amongst other illegal purposes and ends that are contrary to public policy.

Also noteworthy is the era when specific banks deployed as "Market Makers" in view of the negative down trend in the stock and derivatives market. The timely intervention of regulatory authorities mitigated the impact of heavy liquidity out-flows experienced by some banks, and thus negatively affecting their day to day operations. Thus, it came to the light that with the aid of insider information, some banks were able to avoid harsh regulatory sanctions. The elastic effects of the corporate rearrangements exercise came to the light primarily because of sitting government's resolve to adopt the liquidation option rather than bailing out the banks. Unchecked practices of insider dealings usually undermined established policies resulting in corporate failures in diverse respects coupled with the attendant negative macro-economic effects. Hence, the role of corporate regulation via applicable laws and policies cannot be relegated in order to manage the diverse incidences of insider dealings (Abubakar, 2013).

It is not practical to deal exhaustively with every instance of unethical business (insider dealings) and the dynamics of the corporate banking regulations. Hence, the approach adopted in this paper is to purposively construe existing evidences as a basis to expound on fundamental issues relative to non-compliance and part-compliance with applicable laws, codes, regulations and established industry practices.

## 2. REGULATION OF COMMERCIAL BANKS

The dilemma bedeviling Nigeria's banking industry is best exemplified by the Failed Bank and Financial Malpractices in Banks (Recovery of Debt) Act, 2004. The crisis majorly centered on non-fulfillment of credit and loan obligations by identifiable insider actors. Hence, the commercial banking space was evidently eroded by this inappropriate trends, coupled with other species of corporate abuse and unethical practices. The Failed Banks Act was indeed timely and restored some sanctity to the commercial banking environment. It is noteworthy there were other laws in this respect, but due enforcement was relatively lacking to achieve the desired outcomes.

Nigeria's banking industry is regulated in specific respects by notable enabling laws. The applicable laws include the Companies and Allied Matters Act (CAMA) of 2004, CBN Act, 2007, the Banks and Other Financial Institutions Act, 2004 and to some extent the Nigeria Deposit Insurance Cooperation Act, 2006 No. 22 of 1988. The laws in various regards deal with issues like; disclosure of interest by insiders, and the system of CBN off-site surveillance and the on-site audits of banks. A notable feature of the industry is low ethical standard and transparency. These are

manifesting in the rising cases of unwholesome practices being recorded.

The focus of the regulators typically lies in reducing sharp and unorthodox practices, promoting filing of accurate financial reports and timely reporting of unethical practices; strengthening internal governance structures, sanctioning managerial incompetence. In effect, such an outlook will contribute in measurable respects to lowering corporate losses, reduce bank frauds and further highlight the importance of maintaining functional internal control systems.

## 3. BANKING ETHICS: CONCEPTUAL AND PRACTICAL OVERVIEW

Generally, a professional banker stands in a position of trust in relation to the public. It is fiduciary in nature and as such is accountable to specific interests or groups. A banker can also be appropriately regarded as a custodian of individual, group, corporate and national wealth. Typically, bankers are involved with managing the finances of; individuals and corporate entities. The essence of professionalism in banking lies in the ability and competence to give the customer basis for complete trust as well as faultless service. Sustainable banking activities thrive on maintaining public confidence and trust. The bank that lacks such essentials will progressively lose its competitive element or dynamic.

Professionalism requires optimal adherence to the highest standards of ethics and due compliance as required by the prevailing law. It is the fundamental platform for ensuring a robust, effective and sustainable banking system. It thus suffices to say that inspite of the evident regulatory gaps attributable to the commercial banking sub-sector; the actors are still subject to the well-established concept of the ethical compliance. This connotes in certain respects that stakeholders have an apparent right to expect a business to be conducted ethically, and a view to the contrary will harm the corporate entities long-term interests and good will (Duska, 2007).

Interestingly, the prevalence of unethical practices in the banking industry, particularly in the mode of insider dealings, further exemplifies corrupt tendencies attributable to the broader political and socio-economic national context. In the circumstances, regulatory have had to adopt various measures to secure depositors and shareholders funds. The ill-preparedness and negligence of the regulator contributed to the level of distress in industry over time, and this has manifested in low productivity across other sectors which rely on the financial support of the banks in growing their businesses. It is instructive to note that such an outcome negates customary function of governmental regulatory agencies, duly empowered regulate the activities of commercial banks. This can be effectively carried out; in as much as such does not amount to the control and undue interference with the legal business activities of the corporate entities (Akinbola et al., 2013; Nwano, 2013). The frenzy associated with the policy driven recapitalization activities of Commercial Banks (2003-2007), evidently stretched the limit of ethical compliance. This conclusion can be drawn as background incidents unfolded as regards the questionable means

used to secure bank deposits, fraudulent share subscriptions coupled with other unethical practices geared towards securing undue advantage. The constant pressure and influence to maintain a competitive advantage has undeniably tainted the fundamental of the commercial banking environment, thus further impairing the transparency and business confidence index attributable to Nigeria's Business Environment.

This trend of distress assumed a different dimension in the early 2000s. A wave of public share offers and series of mergers and acquisitions was experienced in the Commercial Banking Industry. It was primarily geared at regaining public trust and to achieve some degree of stability in the banking system. A reasonable number of the corporate arrangements did not stand the test of time as was typified by corporate maneuverings on multiple levels with diverse consequences for individual and corporate interests. The intervention of the Asset Management Company of Nigeria (AMCON) as a 'bridge bank' and in taking buying over bad debts of distressed banks has further highlighted the instability within the corporate structure of certain banks. This is evident as AMCON exercises its wide regulatory powers to restore some degree of sanctity to the affected banks.

### 3.1. Insider Dealings: Regulatory Overview

In the legal parlance, who is an insider? An insider by Section 315 of the Investment and Securities Act (ISA) and Rule 110(3) of the Securities and Exchange Commission Rules and Regulations 2013 is a person in possession of price sensitive information and deals on the securities of such Company. The CAMA 2004 Laws of the Federation of Nigeria, Section 111(1) of the ISA 2007 (ISA) prohibits any person who is an insider of a Company from purchasing, selling or otherwise trading in the securities of such company which are offered to the public either for sale or by subscription if he or she has information which he or she knows is unpublished and price sensitive information in respect of those securities. Rule 17 of the Code of Corporate Governance for Public Companies in Nigeria disallows the directors of public Companies, their immediate families, their wives, sons, daughters, mothers or fathers and other relatives from trading in the securities of that company.

According to the provision of Section 116 (1) ISA, the Securities and Exchange Commission's Investments and Securities Tribunal may order any person who is culpable of insider dealing to pay compensation to any aggrieved person for the purchase or sale of such securities. Section 115 of the ISA also makes provisions for criminal sanction against any person who engages in insider dealing to be liable on conviction in the case of an individual to a fine of not <5000 Naira or any amount equivalent to the double of the amount of profit he got or losses he averted by the use of the information or to an imprisonment for a term not exceeding 7 years and in the case of a body corporate fine of not <1 million Naira or amount twice the amount of profit got or loss it averted by the use of such information. The deterrence effect of the stipulated fines is however debatable.

The concept of ethics converges in certain respects with the widely-debated issue of morals or morality. The former can be broadly depicted as conforming to stipulated codes and practices within a

given context. In effect, the term can be regarded as the foundation of personal, corporate and national success. In the more exclusive and corporate sense, ethics encapsulates the minimum benchmarks by which of measuring the competence of individuals involved in the practice of a given profession or calling. The profession of banking is indeed one that is integral to overall national economic development, and as such one which demands maintenance of high and consistent ethical standards. It is in adopting such a high-level trust posture, lies foundation of securing the enduring confidence of the diverse stakeholder base. Thus, it rests on the stakeholders to ensure that the ethical compliance remains an integral part of their business processes. Moreover, regulation has its limits, as even with the considerable level of regulation and scrutiny, avoidance and non-compliance is still very evident.

Insider dealings covers a range of issues such as; non-disclosure of the interest conflicting interest relative the principal actors in a transaction; diversion of assets for personal use and abuse of position abuse to facilitate transactions to the detriment of the corporate interest. Other dimensions entail exploiting weak corporate governance structure for personal gains as well specific forms of managerial abuse. Hence, these dimensions of insider dealings contribute to impairing public confidence, especially in a context where illegitimate use of sensitive market and financial information is left unregulated and is allowed to thrive to the detriment of other stakeholders (Davies, 1997). There are incidences of unwholesome practices being recorded for banks, several banks engage in some sharp and unorthodox practices to achieve compliance with some regulatory requirements.

Certain conducts are classified unprofessional/unethical some are; conflicts of interests, engaging in extraneous activities which interfere with or constrain a bank's primary responsibility, colluding with third parties to inflate contracts. These includes amongst others; analysis of the volume of deposits and evasion of insurance premium, mandatory cash reserve requirements, imposition of previously undisclosed charges on customer's accounts; failure to submit report on dismissed/terminated staff to CBN and allowing proven fraudulent staff to resign, failure to submit report on eligible credit to CBN for necessary audit and monitoring.

It also includes; misuse of information, manipulation or non-disclosure of material information to derive some benefit or avoid liability, running down competitors through deliberate misinformation. Misuse of various financial derivatives, deliberate rendition of inaccurate returns the regulatory authorities with intent to mislead, misuse of confidential information gained through banking operations. These amongst others, are forms of unethical practices which escalate the risks attributable to the banking system.

## 4. INSIDER DEALINGS: STAKEHOLDERS PERSPECTIVE

The full effects of insider dealings in Nigeria's commercial banking industry came to the fore in 2009 as the apex bank rescued



eight banks, associated with non-performing loans estimated at N3 trillion. The CBN at the time had injected over N620 billion in the banks, dissolving the management board and appointing a new team to manage the affairs of the affected banks. According to the regulator, the non-performing loans due largely to exposure to capital market trading and the oil and gas sector had negatively impacted on the shareholders' funds. The sharp and consistent decline in global oil prices (2015-2016), coupled with the negative impact on the value of the local currency and changes in governmental policy will further test the sanctity and veracity of processes in the existing commercial banks. This outlook is instructive in view Nigeria's overreliance on oil revenues and its associated risks and collateral damage, especially in periods of lower earnings from crude-oil sales. Moreover, such negative or unfavorable indicators are to further test the credibility of the institutions operating in the financial sector of the economy. Notably, the new managements set up to run the affairs of the rescued banks were then mandated to seek core investors that would bring in new expertise and capital to strengthen the banks. However, shareholders of some of the banks went to court challenging the legality of the CBN's action.

The CBN has been relatively successful in facilitating the establishment and functioning of the AMCON. Specifically, it has provided an appropriate option to handle the issue bad debts in a fiscally responsible and sustainable manner. It is also noteworthy, that the asset management and recovery centric institution, has taken up over N1.7 trillion of non-performing loans in the books of the banks, replacing it with tradable bonds. Multiple and various forms of corporate arrangements and re-arrangements have occurred since the advent of AMCON as the banks seek to retain their relevance in commercial banking environment.

For organized labor, liquidating virile 'rescued' banks were rather hasty and could hurt the economy deeply. In fact, for them it is tantamount to carrying out anti-national policies over which they requested presidential intervention. The workers under the aegis of Association of Senior Staff of Banks, Insurance and Financial Institutions (ASSIBIFI), Nigeria Labor Congress affiliate, urged the supervising Ministry and the Presidency to critically look at all the current issues in the banking industry patriotically rather than leaving them in the hands of uninformed and biased regulators (The Nigerian Voice, 2011). The National President of the Union at the time lamented that the policies being pursued by the CBN presently would rather create more chaos for the Nigerian economy. Moreover, such a posture by the CBN had the potential of escalating public distrust in the stability and viability of the banking industry, and thereby constraining financial standing of the affected banks (The Nigerian Voice, 2011). The ASSIBIFI president said that the utterances of the leadership of the CBN on the state of these banks were questionable as it could be considered that there was a preconceived intention to liquidate the banks irrespective of their financial health.

It was also noted by the leader of the workers' union that, one of the banks was declared illiquid for financing government-guaranteed projects. The disclosure issue is a recurring issue that continues to put the commercial banking system in bad light. This is evident on

the part regulators and operators as both seek to promote their own interests to the detriment of the largely undiscerning public. It is important for all stakeholders to synergize in this respect, coupled with the much needed political will to ensure policy consistency and implementation (The Nigerian Voice, 2011).

## 5. A BRIEF JUDICIAL VIEWPOINT ON INSIDER DEALINGS

In the case of Securities and Exchange Commission v. Texas Gulf Sulphur Company (1966); it was decided that any person in possession of inside information should either disclose the information or abstain from trading on such information. Also, instructive in this regards; is the case of United States v. Carpenter (1986); where the Court upheld the conviction of the defendants who received confidential information from a journalist rather than from the Company contrary to the mail and wire fraud statutes. Similarly, in the decided case of United States v. O'Hagan (1997) where O'Hagan utilized inside information to buy call options on Pillsbury stock and made profits of over \$4 million. The court rejected O'Hagan claim that he owed no fiduciary duty to Pillsbury and that he did not commit any fraud and the court upheld his conviction.

In Nigeria, on January 6, 2014, the Securities and Exchange Commission's Administrative Committee overturned the registration of Sterling Registrar Limited, a division of Sterling Bank PLC for unauthorized apportionment of shares of Japaul Oil and Maritime Services PLC. It also barred Kalstead Farms Investment Limited and five other persons, with the staff of sterling registrar from involving in capital market activities for a given period. The requisite fines levied and the additional charges were imposed, considering each day of the unauthorized allotment (Abugu, 2015).

## 6. CONCLUSION AND RECOMMENDATIONS

The trend of insider dealings in Nigeria's commercial banks is quite evident. It has also evolved in certain respects as the processes and practices become more integrated and complex. Recognition of the negative implications of insider dealings for the banking sub-sector and the wider economy has reinforced the essence of due regulation. However, in order achieve optimal returns, it is important for all the stakeholders to engage more effectively to promote the goals that are productive and sustainable in the long-term. It is instructive to consider the peculiarities of Nigeria's Banking Industry. Specifically, the banks are gradually integrating into the global financial markets and are thus more prone to a wider spectrum of risks which they are sometimes ill equipped to effectively address. Hence, the need for an approach that is; proactive, interventionist and protects the overall sanctity of the industry. The lessons from other mature climes must also be adapted with circumspect bearing in mind variances in the operating environment.

The CBN must lead the course to protect shareholders' interests who are the primary victims of the negative effects on insider

dealings. As the apex bank, it should be duly involved in the process, but ensuring fair treatment of all the banking operators. As a regulator, it is expected to design realistic benchmarks, coupled with ensuring effective monitoring and due compliance with established guidelines. A practical whistle blowing framework must be established to facilitate exposure and mitigate the trend of insider dealings. Such a measure would contribute in the detection and prosecution of person involved in insider dealing, especially as regulators are not aware of the commission of the crime which occurs internally within the corporate context.

The regulatory interventions by the CBN are consistent with the essence of the well-established management theoretical foundation, that is, the stakeholder theory. Specifically, mitigation of insider dealings by way of corporate regulation reinforces the standpoint that; the corporate body was created to serve multiple interests and stakeholders who have a legitimate stake in the organization's performance or output (Mercer, 1999). The scope of stakeholders can in effect be enlarged to capture any person or collective of persons that is directly affected or may be potentially affected by the achievement of the organization's objective (Freeman, 1984) Hence, a deviation from appropriate pathways to achieve the corporate goals necessitates some form of intervention to protect the matrix of interests associated with the corporate entity. Essentially, the goal is to ensure an effective balancing on the rights and obligations attributable to persons or groups expressly or implicitly affected by the performance of the organization (Sayre-McCord, 2000).

In more practical terms, stakeholder rights are centered on the progressive negotiations, contextual compromises, agreements as well as compliance on multiple levels amongst the requisite parties. Thus, where corporate trends, practices or outcomes cannot be captured within recognized, appropriate and measurable parameters, such can be duly considered as being for the benefit or gain of identifiable stakeholder. This is instructive, as there are indeed legitimate options and processes for deriving and sustaining value, wealth and rewards for the multiple interests connected with corporate entity. The focal point should thus be to advance and entrench the acceptable and legitimate avenues for creating corporate wealth as a veritable means to diminish the incidences of insider dealings amongst other unethical corporate practices.

There is need for application severe penalties for the offence considering the consequences and prevalence. The training and equipping of the law enforcement agencies and statutory regulatory authorities is also necessary for insider dealings detection, investigation and prosecution. Severe criminal sanction may fail to serve as deterrence, if the suspected insiders are not arrested for prosecution and punishment. In effect, a contrary posture will only escalate the fears of the shareholders and further dampen public trust

in the commercial banking system. Nigeria, can ill afford to project a culture of condoning unethical practices, as the banks are fundamental to the recovery of the socio-economic indicators, currently (2017) experiencing a notable decline. Instructively, the issues captured above further highlight the scope of the corporate governance dilemma bedeviling Nigeria's commercial banking industry.

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