Payment Discipline Depends on Management Ethics

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The main aim of the study was to identify if management ethics have a positive impact on payment discipline. Our sample includes 273 Slovene enterprises, which represent 9.1% of 2978 Slovenian enterprises with 10 or more employees, selected from the database of the Slovenian rating agency I d.o.o. To determine management ethics, we used the Corporate Ethical Virtues measurement instrument questionnaire. The data concerning average late payments were also obtained from the database the Slovenian rating agency I d.o.o. We conducted a factor analysis using the enter method. We confirmed that the influence of management ethics have a positive impact on average payment delays expressed in days.

Key words: management, ethics, late payments

Introduction

'A company with unethical behaviour cannot become (nor remain) permanently successful' (Belak, Thommen, and Belak 2014, 84). Indeed, ethical behaviour in the company is a source of competitive advantage (MacDougall et al. 2015). From the theoretical point of view, 'ethics must deal both with companies' social and economic issues, with the behaviour of all stakeholders of the company' and 'with the relations among companies' stakeholders on all organisational levels, among interest groups of internal and external stakeholders of the company' (Belak, Thommen, and Belak 2014, 84). Sims (1992) predicted in the 1990s that companies in this century would undergo numerous changes and encounter many challenges greatly influencing the dynamics and effectiveness of companies. He identified six key challenges, decisive for the survival and progress, or the failure of companies. Among these six challenges, he mentioned ethical behaviour. According to him, many managers and experts in social sciences are concerned about the ethics crisis undermining the competitiveness of the West and consider unethical behaviour a cancer corroding society and something that is present in a large number of companies and outside of them. Just as different individuals react differently to ethical issues, there are also differences in companies' reactions to ethical issues (Logsdon and Yuthas 1997; Peterlin et al. 2011). If companies want to achieve long-term success, they must earn reputations as credible and trustworthy partners and the prerequisite for this is their ethical behaviour (Duh, Belak, and Milfener 2010).

Nevertheless attention to the business ethics have been increased over the last few decades (Tenbrunsel and Smith-Crowe 2008), ethics are not as influential as they should be. Between 1975 and 1985, 62% of companies from the Fortune 500 list were involved in some kind of forbidden activity (Etzioni 1985). Sims (1992) wrote in 1992 that unethical behaviour by companies was shockingly frequent. Circumstances have not changed considerably in the meantime. Research conducted in 2008 on a sample of 1,752 managers and employees from five countries showed that 16% of participants had noticed blackmail, 15% had noticed discrimination, 11% thievery and 7% forgery of cost reports in the last 12 months (Kaptein 2011). Another study, which was also conducted in 2008, included 5,065 American managers and employees and showed that 74% had noticed unethical behaviour in their company in last 12 months (Kaptein 2011). Based on these results, we can conclude that companies do not take enough account of ethics and laws. Applying business ethics should be part of the change in company policy and should be present at all levels of the control and management process, both at the implementation level of that process and working routine (Belak and Milfener 2011).

Wolfe (1998) explained that managers have developed ways of thinking (sometimes not even being aware of it) that promote unethical behaviour. In this regard, he presented the mentality (called the 'bottom-line mentality') where the only important value is financial success. This mentality encourages short-term solutions, which are good from a financial point of view, despite the fact that they cause difficulties for others in company or for the company as a whole. Such a mentality promotes the irrational belief that indeed everything is a money game where moral rules are only a barrier to the achievement of set and desired financial success.

'Decisions on ethical issues are complex and influenced by individual differences, as well as situational limitations' (Kurtines 1986,

790) and 'pressures within companies are the best predictor for ethical or unethical behaviour' (Ferrel and Gresham 1985, 90). The circumstances in which companies operate are often hostile and highly challenging; therefore, it is difficult to overcome tendencies to make ethical compromises, especially when resources are limited, and there is no room for errors (Longnecker 2006). Examples of such situations include time constraints, lack of money, mind-set that the compromise in ethical behaviour can be decisive for the company's survival or failure, unclear limits between ethical and unethical behaviour, as well as hiding unethical behaviour from the public (Morris et al. 2002).

The risk from adverse effects provoked by the lack of payment discipline is significantly increased in times of economic crisis (European Parliament and the Council 2011), and this is reflected in the decrease of investments, reduced trading volume and increased interest rates (Lin and Martin 2010), and it is harder to obtain sufficient financial resources to ensure liquidity (Vojinović, Mikac, and Oplotnik 2013). The directors of companies, who often justify unethical behaviour to themselves (Dean, Beggs, and Keane 2010), e.g. a lack of payment discipline, have an important role in this issue. In addition, companies often derive no benefit from ethical behaviour (Dean, Beggs, and Keane 2010).

The lack of payment discipline, which is defined as late payments and debtors' failure to settle their liabilities (Commission of the European Communities 2009), is a massive problem all European companies encounter, and it causes the greatest difficulties mostly among small and medium-sized companies. Managers are aware that the effect is greater if one euro is saved than if one additional euro is earned (Rottig, Koufteros, and Umphress 2011), and companies with late payments save on interest payments, since, as a rule, late payments are a free source of financing. If late payments are actually intentional, according to 63% of companies (Intrum Justitia 2011), then this is very unethical. Our assumption is that precisely the management of the company is responsible for this.

Heavy administrative and financial burdens are placed on companies because of excessive payment periods and late payments (European Parliament and of the Council 2000). The situation in Europe regarding payment discipline is presented in tables 1 and 2.

In Slovenian companies late payments are the main reason for the lack of payment discipline (Prašnikar, Pahor, and Cirman 2010). This phenomenon can be defined as an unfair commercial practice among companies (Commission of the European Communities

TABLE 1 Average Payment Terms Allowed to Customers, Average Time for Actual Payment and Average Payment Delay in European Countries in 2015 for Business to Customers Market (B2C), Business to Business Market (B2B) and Business to Public Market

Country	Average payment terms allowed to customers			Average time for actual payment			Average payment delay		
	(1)	(2)	(3)	(1)	(2)	(3)	(1)	(2)	(3)
Austria	17	21	25	18	25	32	1	4	7
Belgium	21	31	42	23	44	69	2	13	27
Bosnia-Herzegovina	15	19	25	18	31	42	3	12	17
Bulgaria	16	30	33	17	39	52	1	9	19
Croatia	29	33	37	38	48	48	9	15	11
Czech republic	17	21	23	17	26	29	0	5	6
Denmark	16	21	22	19	25	27	3	4	5
Estonia	10	15	18	12	20	21	2	5	3
Finland	13	18	18	15	23	22	2	5	4
France	23	38	43	33	51	62	10	13	19
Germany	14	18	19	13	17	19	0	0	0
Greece	16	26	35	21	31	49	5	5	14
Hungary	18	22	28	20	28	42	2	6	14
Ireland	18	23	24	18	27	28	0	4	4
Italy	33	55	79	48	80	144	15	25	65
The Netherlands	19	23	23	19	29	32	0	6	9
Norway	18	21	26	21	27	32	3	6	6
Poland	22	22	22	33	32	33	11	10	11
Portugal	34	49	55	40	70	94	6	21	39
Slovakia	15	19	18	12	23	23	0	4	5
Slovenia	17	27	30	20	36	35	3	9	5
Spain	44	56	70	45	70	103	1	14	33
Sweden	22	27	29	24	31	32	2	4	3
Switzerland	26	28	30	33	37	40	7	9	10
United Kingdom	15	18	18	15	21	24	0	3	6

NOTES Column headings are as follows: (1) customers market, (2) business to business market, (3) business to public market. Adapted from Intrum Justitia (2015, 20–48).

2008). Therefore, we assumed that the ethics of the management influenced the timely or delayed settlement of the company's liabilities to suppliers.

Many authors have confirmed the influence of management on the ethical behaviour of companies (e.g. Ferrel and Gresham 1985; Posner and Schmidt 1992; Wimbush and Shepard 1994; Kaptein

TABLE 2 Average Payment Delay in Main Industries in 2013 for Business to Customers Market (B2C), Business to Business Market (B2B) and Business to Public Market

Industry	Average payment delay		
	B2C	B2B	Public
Professional services	12	15	16
Construction	17	25	33
Manufacturing	12	22	26
Education	13	13	12
Media	14	20	17
Business services	12	17	17
Wholesale & Retail	9	12	18
Real estate	6	10	15
Telecom	11	14	24
Transport	10	18	19
Financial services	10	10	12
Utilities	10	12	17
Health care industry	25	17	35

NOTES Adapted from Intrum Justitia (2013, 11–23).

2011; Hawkins, Lewis, and Amos 2012). If we observe payment discipline as a counter-norm, then the ethical behaviour of management should influence the payment discipline of the company.

Despite numerous studies on the general issue of ethics among managers, our systematic review of literature reveals a gap in the research and the evident need for empirical study of the relationship between management ethics and payment discipline. The study presented in this article was conducted within a working environment and attempts to narrow this gap.

The goal of this article is to determine if management ethics influences companies' financial discipline. The paper is structured as follows. After the introductory part of the paper, the second part of the paper explores the methodology of the research. Third part of the paper discusses results. Fourth part of the paper includes discussion. Finally, managerial implications and conclusions are presented.

Method

SAMPLING AND SAMPLE

A total of 2978 Slovenian micro, small, medium and large enterprises were randomly selected from the database of the Slovenian rating agency I d.o.o. Micro-sized enterprises is defined as enterprises with less than 10 employees, small enterprise is enterprise from 10 to 50 employees, medium from 50 to 250 employees and large enterprise includes more than 250 employees.

Persons responsible for accounting or financial data from these companies were contacted via email with a request to participate in an online survey. In addition to the answers about ethical culture, respondents only had to provide the name of the company, so that the data about a company's ethical culture could later be compared with the data about its payment discipline. Average payment delay was calculated using the Dun & Bradstreet rating agency methodology (average delay was calculated taking into account a sample of invoices).

Our sample includes 273 Slovene enterprises, which represented 9.1% of all companies invited to take part in the survey. The share of companies with late payments is 64.6% and the average late payment is 8.07 days. According to the company size there were 26.6% micro, 35.1% small, 18.1% medium and 20.3% large size companies.

DESCRIPTION OF THE MEASUREMENT INSTRUMENT FOR MEASURING MANAGEMENT ETHICS

To determine the management ethics, we used 10 items for measuring management ethics from the measurement instrument for assessing the ethical culture (Kaptein 2008). We used item from Kaptein's measuring instrument for determining the ethical culture (2008) since his measuring instrument is developed, implemented and valid measuring instrument. Our measuring instrument consisted of claims on which the respondents gave an assessment of agreement or disagreement with the help of Likert 6-point scale.

In order to avoid mistakes due to the translation process (original questionnaire was in English, but the research was conducted in Slovenian language) we translated measurement instrument first into Slovene, and then back into English. Then we compared both sets of items (the original ones with items translated back into English) and finally, we test our measurement instrument on a small sample and we confirmed that no additional changes to the item were needed.

PROCESS DESCRIPTION

An electronic questionnaire with a request to participate in an online survey was sent via email to the people responsible for accounting or financial data. The first part of the questionnaire, which also asked for the name of the company so that the data could later be compared with the data about its payment discipline, gathered information about the companies' management ethics, measured using ten statements from the Corporate Ethical Virtues measurement instrument (Kaptein 2008).

DATA ANALYSIS

For testing reliability of the questionnaire the criterion of internal consistency Cronbach's alpha Cronbach (1951) was used.

Whether our measuring instrument meets the criterion validity of the construct (whether items in the measuring instrument have one or more common category of higher order – construct) was checked with factor analysis.

Since the average delay was expressed in days (tense variable) and because we assumed that between it and the independent variables is a linear dependence, we have models of payment discipline formed by linear regression analysis. In linear regression, we analyzed the multicollinearity. It is generally accepted rule says that the problem of multicolinearity factors indicate an increase in variance is greater than 10 (Gujarati 1995, 339) and tolerance of less than 0.1 (Lin 2006, 422), some authors have labelled as troublemakers factors increase the variance of greater than 4, and tolerance of less than 0.25 (O'Brien 2007, 674).

Results

FACTOR ANALYSIS, RELIABILITY, AND VALIDITY

Using factor analysis variability a potentially lower number of unobserved variables called factors is described. With the factor analysis, we get one factor, which contains the variables of management ethics. The factor contains nine variables that are substantial in this set. The variable 'My supervisor fulfils his responsibilities' was discarded due to the lack of communalities.

Bartlett's test was statistically significant ($\alpha = 0.000$) and the value of KMO test came to 0.712, which makes the data suitable for factor analysis. The construct 'management ethics' ($\alpha = 0.956$) was analysed and confirmed with factor analysis. Table 3 presents the factor structure and loadings.

From the factor analysis, using the PAF method and varimax rotation, we get one factor, named 'management ethics,' which has an eigenvalue of greater than 1. Only one item was abandoned: 'My supervisor fulfils his responsibilities.' All of the items included in the factor explained 74.09% of the total variance.

TABLE 3 Factor Analysis

The Board and (senior) management sets a good example in terms of ethical behavior.	0.895
My supervisor communicates the importance of ethics and integrity clearly and convincingly.	0.891
My supervisor does as he says.	0.887
My supervisor would never authorize unethical or illegal conduct to meet business goals.	0.884
My supervisor sets a good example in terms of ethical behavior.	0.867
The Board and (senior) management communicates the importance of ethics and integrity clearly and convincingly.	0.849
My supervisor is honest and reliable.	0.836
The Board and (senior) management would never authorize unethical or illegal conduct to meet business goals.	0.820
The conduct of the Board and (senior) management reflects a shared set of norms and values.	0.812

TABLE 4 ANOVA

Item	Sum of Squares	df	Mean Square	*F*	Sig.
Regression	951.017	5	190.203	3.320	0.006
Residual	15126.450	264	57.297		
Total	16077.467	269			

NOTES Predictors: (constant), management ethics, quick ratio, debt to equity ratio, return on equity, three-firm concentration ratio. Dependent variable: average payment delays.

LINEAR MULTIPLE REGRESSION

With multivariate regression analysis, the descriptive measures for each variable were calculated: measures of correlation, parameter values of the regression model, table of variance analysis, parameter estimates of regression function, values of related tests of independence of parameter estimates, and values of remains. Analysis was conducted on how the independent variables influence the dependent variable. When the regression model was accepted and the independent variable values examined, we were able to forecast the emergence or values of dependent variables.

The ANOVA analysis provides the statistical test for overall model fit in terms of the F ratio. The total sum of squares (190.203) is the squared error that would accrue if the mean of management ethics has been used to predict the dependent variable.

The linear regression model with enter method is presented in table 5. In this model variables management ethics, quick ratio, debt to equity ratio, return on equity and three-firm concentration ratio

TABLE 5 Linear Regression Model Using Enter Method

	Unstand. coeff.		Std. coeff.	t	Sig.	Collinearity stat.	
	B	Std. err.	β			Tolerance	VIF
(a)	7.054	1.010		6.986	0.000		
(b)	−1.106	0.469	−0.143	−2.358	0.019	0.968	1.033
(c)	−0.124	0.195	−0.039	−0.633	0.527	0.950	1.052
(d)	0.193	0.109	0.111	1.777	0.077	0.916	1.092
(e)	0.764	1.313	0.036	0.582	0.561	0.943	1.061
(f)	−4.940	1.747	−0.170	−2.828	0.005	0.987	1.014

NOTES Row headings are as follows: (a) constant, (b) management ethics, (c) quick ratio, (d) debt to equity ratio, (e) return on equity, (f) three-firm concentration ratio. a. Dependent variable: average payment delays.

can explain 5.9% of the variability of average payment delays. In the regression model in table 5, there are no multicollinearity issues (all variances are higher than 0.25 and all factors of increased variance are lower than 4). Management ethics is significantly statistically related to average payment delays expressed in days ($\beta = -0.143$, $p < 0.05$). With regards to the control variables, only a significant negative relationship between the three-firm concentration ratio and average payment delays expressed in days is statistically reliable ($\beta = -0.170$, $p < 0.01$).

Discussion

The aim of this article is to determine if management ethics influences companies' financial discipline. This study was constructed on valid models and contributes to theory on management ethic and payment discipline.

With the factor analysis, we get one factor, which contains the variables of management ethics. The factor contains nine variables that are substantial in this set. The variable 'My supervisor fulfils his responsibilities' was discarded due to the lack of communalities.

Through regression analysis, we examined the relationship between management ethics and financial discipline. Using the enter method, we yield a model that is statistically significant, with which we explain 5.9% of the variability of the dependent variable. The hypothesis regarding the positive impact of the management ethics on payment discipline was confirmed, since management ethics have impact on average payment delay.

The role of managers in creating an ethical working environment in a company is very important. They encounter different ethical dilemmas in their work and must be able to solve them successfully. Solving such complications is often difficult, since they are required to take decisions where they cannot refer to laws, regulations, statutes, and absolute truths. Namely, ethical dilemmas always cast doubts, and because of them, some people can be strongly affected or harmed. The consequences of unethical behaviour are often reflected in the loss of trust and goodwill. Loss of trust has a significant impact on the business operations of a company as it changes the attitude to work which in turn affects creativity, productivity, motivation and/or the workflow and climate in the company, which is also reflected in stunted communication and decreased commitment and loyalty. The loss of goodwill also has a high price, especially if the information about unethical behaviour is made public. Unethical behaviour can easily damage a reputation that was difficult to earn. The reputation of a company is built up over years, but can be destroyed in a single day by irresponsible behaviour (McAlister 2003, 46; Tierney 1997, 18–34).

Conclusion

Considering the results of our research, we suggest the improvement of payment dimensions by strengthening the management ethics. This can be achieved with training. In light of the results of our research, we suggest that managers behave ethically so they can also improve the financial discipline of the companies they work for. Here, managers should follow this sequence (Tierney 1997, 76–96):

1. They have to take the decision to act ethically. They need resources to create an ethical atmosphere. In addition, managers must concern themselves with values and include everyone in the creation of an ethical work environment, and at the same time, they must set an example to follow.
2. Managers must be aware that they, with the leadership position, set an example for others through their actions and values. Managers are a role model simply due to their position and they have a huge impact on other members of the company. The role of managers affects relations with the people they do business with, and with the people who are their subordinates, whose work must reflect quality and accuracy if they want to meet the expectations of the manager who assigned them a task. The manager's assessment and evaluation of subordinates influences their career and salary. If managers want to create an ethical climate, they must set an example to others with their values.

3. Managers must take responsibility to encourage ethical behaviour. Responsibility for promoting ethical behaviour starts at the top. Words alone are not enough.
4. They must provide their own definitions of ethical behaviour. Managers should place ethics high up on the list of priorities in business operations in all areas, e.g. when hiring people, in advertising, accounting, research.
5. Managers must articulate their values. They must be aware of their values, which are an example for employees, and be able to articulate them.
6. Managers must educate employees about ethics. Some sort of education is also required to create an ethical environment. Employees must also be informed about the business of the company, as well as about the company's business ethics. Managers must encourage ethical thinking and demonstrate its importance to employees.
7. They must encourage open communication. Managers must promote communication among employees and they must feel that they can openly discuss criteria, values, and ethics, without fear of consequences.
8. Consistency also matters. Managers must have at their disposal resources to give warnings for unethical behaviour or punish such actions. If there are no consequences for unethical actions, this indicates that what is preached is not practiced. Therefore, respect for criteria must also be very visible when rewarding. Ethics, in addition to excellence, is crucial for the success of the company.

Taking into consideration results of our research, it would be necessary to find appropriate forms of the incorporation of ethical behaviour-related training in business studies (in the cases in which such contents have not yet been included in curriculum). In this way, the moral judgement of future managers and financiers would be improved.

In the case of any research in the future, we propose comparisons between results obtained in different countries. Taking into consideration that there are considerable differences in payment discipline throughout Europe, any research on comparisons between the impacts of ethical climate and ethical culture in different countries with varying levels of payments discipline would be welcome. Within such research to be simultaneously conducted in more countries, it would be reasonable to verify the impact of national culture, defined as a 'set of beliefs and values that distinguishes one nationality from the other and it is extremely stable' (Lažnjak 2011, 1018), on payment discipline.

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