An Integrative Governance Model for Understanding Ethical Behaviour: Evidence from Malaysian GLCs

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Abstract

While governance, through strong legal and regulatory institutions has been the norm to attract and protect investments, its effectiveness in reducing unethical business behavior such as corruption, fraud and bribery is questionable. The solution of further strengthening governance through legal and regulatory institutions through Dodd-Frank Wall-Street Reform and Consumer Protection Act after the 2007/2008 subprime mortgage crisis in the US has yet to show any results in enhancing ethical behavior. Therefore in this article we argue that apart from external governance, organization’s internal governance needs to be strengthened to curb unethical business behaviors in organizations. Interview data collected from several government linked companies (GLCs) in a developing country confirm our arguments on the lack of effectiveness of external governance. We therefore propose an integrative governance model that encompasses both external and internal governance factors influencing ethical behavior. Using PLS, the model is then empirically tested on a sample of 113 respondents from a government linked company. The empirical results shows positive impact of both external and internal governance on ethical behavior.

Keywords: Governance, Ethical behavior, Economic Development, Fraud
Introduction

Governance, through strong legal and regulatory institutions has been the norm to attract and protect investments. Investments by business organizations lead to capital accumulation that foster innovation driven GDP growth. Corporate taxes in turn can be invested by governments to accelerate economic development and prosperity of its citizens. Consequently, in accordance with conventional financial development wisdom, building and strengthening legal and regulatory institutions that protect investors in developing nations as espoused by World Bank is the key to propel economic development and wealth creation (Roe and Siegel 2011). These legal and regulatory institutions are rules, practices and organizations that govern an economy (Johnson and Mitton 2003).

Yet, strong governance through legal and regulatory institutions alone was found to be insufficient to curtail 2007/2008 unethical subprime business conduct that triggered an economic recession in US. The solution of further strengthening legal and regulatory institutions through Dodd-Frank Wall-Street Reform and Consumer Protection Act (Smith and Muniz-Fraticelli 2013) has yet to show its fruits in reigniting sustainable growth especially in US.

Governance through strong legal and regulatory institutions in developing nations like Malaysia has also not been able to reduce unethical business conduct in particular corruption, fraud and bribery. We believe that prevailing paradigm of internal governance driven by ‘tone from the top’ in business organization alone is ineffective as was evident from 2007/2008 subprime crisis in US. This skepticism of the efficacy of ‘tone from the top’ is reflected by fines of $150bil imposed on firms from diverse range of markets since 2009 (Wall Street Journal 2015a) and Federal Reserve Chairwoman, Janet Yellen’s characterization of these fines as “really brazen violation of law” (Wall Street Journal 2015b). A paradigm shift in internal governance need to take place that puts the onus of governance on all employees of an organization, that is, bottom-up governance and not merely on its top management’s, top down governance approach. Ostom’s (2010) work on management of common resource pool showed that community bottom-up governance can sustain its common resource pool even in
the absence of strong legal and regulatory institutions or in the presence of weak legal and regulatory institutions.

A strengthened internal governance by business organizations can complement strong external governance through legal and regulatory institutions. The fact that unethical business behavior persists despite concerted legal and regulatory enhancements may explain a large body of research over the last decade in particular that looks into what organizations can actively do to complement the regulators’ efforts. These include research on values, leadership, organization culture (Victor and Cullen 2006, Williams, 2011) which in essence constitute aspects of internal governance. Unfortunately, no research to date brings all these elements of internal governance and external governance together. External governance effectiveness depends on a combination of factors acting in concert to foster norms of ethical business behavior. These factors include clear laws and regulations, an effective monitoring mechanism through audits to check for compliance to laws and regulations and enforcement of laws and regulations when there are breaches thereof as well as having in place effective behavioral change mechanism such as trainings to foster compliance to laws and regulations. Similarly, in the case of internal governance, its effectiveness depends on an equivalent combination of factors acting in concert within an organization. This research seeks to address this gap by proposing an integrative model of governance that incorporates both internal governance and external governance to foster ethical behavior. The study will focus on government-linked companies (GLC) as they account for the majority 49% of market capitalization of Kuala Lumpur Composite Index (KLCI) (Putrajaya Committee on GLC High Performance Transformation, 2009) and play a prominent role in Malaysia’s economic development. Malaysia’s government through its New Economic Policy (NEP), aspires to build ethnic Malay economic dominance through its government-linked companies (GLC) by primarily reducing the foreign business firms’ dominance of the Malaysian economy (Heng 1997; Pepinsky 2007; Stafford 1997; Yacob & Khalid 2012; Uddin & Uddin 2012). This will also be the first attempt to study the integrative governance model in relation to how cultural-cognitive institution of the State influences the internal governance and external governance that affect ethical behavior of GLC.
This research contributes to literature by proposing an integrative model of governance that combines internal governance and external governance that are required for ethical behaviour. The research empirically validates components of internal governance and external governance that influences ethical behavior. In addition, it contributes to literature by proposing suitable measures for both internal governance and external governance. External governance components includes laws and regulations, auditors that monitor compliance to laws and regulations, regulatory enforcement of laws and regulations and competitive market behavior of business organizations that reflect the spirit of adherence to laws and regulations. Internal governance components includes ethics based core values, feedback monitoring system of compliance to core values, performance system motivation to comply with core values and corporate governance behavior of organization’s employees that reflect core values.

The paper is divided into four parts. In the first part, the Malaysian context for research is provided. In the second part, relevant literature related to governance and ethical behavior is reviewed. In the penultimate part, mixed methods research methodology is elaborated and in the final part, a case will be presented for strengthening internal governance to complement external governance in improving ethical behaviour.

Malaysian Context

Malaysia, like most developing nations, is dependent on foreign direct investment (FDI) to accelerate its economic development. Malaysia’s New Economic Model (NEM) aspires to transform Malaysia into a high-income nation by 2020 through focus on innovative processes, cutting edge-technologies reliant on skilled talent and high-value operations primarily through private sector and foreign direct investment (FDI) to foster high economic growth and development (NEAC 2010). Building and strengthening legal and regulatory institutions that protect investors in developing nations as espoused by World Bank is the key to propel economic development and wealth creation (Roe and Siegel 2011). These legal and regulatory institutions are rules, practices and organizations that govern an economy (Johnson and Mitton 2003). However, Malaysia has been having persistently high levels of corruption despite various efforts to strengthen its legal and regulatory institutions to combat corruption (Siddiquee 2010). Malaysia’s rating in the latest 2015 Transparency
International (TI) Corruption Perception Index (CPI) report has worsened, where it fell 4 places in rank compared to TI’s 2014 report (Malaysian Insider, 2016). Multinational corporations (MNC) especially from the US and Europe may be wary of investing in Malaysia for fear of being charged under the US Foreign Corrupt Practices Act and its EU equivalent, which could delay its goal of achieving high income developed nation status by 2020.

**Literature Review and Hypotheses Development**

**Institutional Theory**

According to Institutional Theory, formal and informal institutions exist to serve the purpose of establishing enduring practices that constrain policies (Cooter and Shaefer, 2010). Institutions’ governance role include social and legal norms that punish rule breakers as well as organizations that sustain them (Cooter and Shaefer, 2010). Institutions are normally associated with 3 pillars namely legal and regulatory pillar, normative pillar and cultural-cognitive pillar (Alexander 2012). The legal and regulatory pillar, as represented by legal and regulatory institutions, a formal pillar, focuses upon conformity to sets of rational rules often written in legal terms of law (Scott 2001) in order to reduce uncertainty of unknown (North 1990). The normative pillar, an informal pillar prevailing in any organization including business organizations such as GLCs, defines organization goals and objectives and the appropriate way to pursue them (Scott 2001) in accordance with socially determined behavior expectations rooted in morals and obligations ((Alexander 2012). The cultural-cognitive pillar, represented by the ruling political party constituting the State, an informal pillar, refers to shared conceptions of social reality and frames through which meanings are made (Scott, 2001) in accordance with these societal actors creating a common frame of reference or categories in order to understand or make sense of the world (Alexander, 2012). These institutions’ governance role i.e. controlling, influencing or regulating behaviours will affect ethical behavior of employees working in business organizations.

These institutions play a critical role in economic development of nations. In this context, building and strengthening legal and regulatory institutions that protect investors as espoused by the World Bank is the key to propel economic development and wealth creation (Roe and Siegel 2011). These legal and regulatory
Institutions are rules, practices and organizations that govern an economy (Johnson and Mitton 2003). Every developing nation including Malaysia wants to emulate the rapid industrialization of the developed western nations such as Britain and Germany that brought developed nation status and prosperity to their citizens. A developmental state, constituting cultural-cognitive institution, refers to the nature of economic development policy a state adopts to achieve developed nation status. There are different institutional frameworks that nations use in pursuit of sustainable developmental state (Hsu 2012). The first proto developmental state includes Listian policy paradigm, Smithian free trade, Ricardian comparative advantage paradigm and Gerschenkron’s State as surrogate entrepreneur (Hsu 2012). The second is based on Weber’s conception of developmental state suited for late industrializers (Hsu 2012) such as Japan, Taiwan and South Korea. For Weber, economic policies of State must serve power political interest of nation whether through direct intervention in economic life or freeing economic forces of nation for their autonomous development (Weber 1994). Malaysia chose direct intervention in economic life through its GLCs (Heng 1997; Pepinsky 2007; Stafford 1997; Yacob & Khalid 2012; Uddin & Uddin 2012). However, Weber (1994) cautioned that aspiring to attain economic power for the State and seeking to advance the career of political leadership, constituting key societal actors of cultural cognitive institutions, do not always coincide. Consequently, Weber (1994) calls for politically mature leaders, constituting key societal actors of cultural-cognitive institutions, to place the goal of achieving enduring economic and political power for the nation above all other interests (Weber 1994) including their personal or party goal of clinging on to political power. In the absence of such politically mature leaders, Weber calls for the role to be played by modern substantive-rational state bureaucracy (Hsu 2012) as was emulated by Japan, South Korea and Taiwan that led to their rapid industrialization, economic growth and prosperity (Stubbs 2009; Lee & Lee 2015). The Malaysian state, constituting cultural cognitive institution, attempted to emulate economic success model of Japan (Furuoka 2007) from early 1980’s to 2003 (Hsu 2012) without much success as Malaysia failed to follow Weberian substantive-rational state bureaucracy model that led to Japan’s economic success (Furuoka 2007). Instead, Malaysia’s developmental state model was nationalistic and anti-West (Furuoka 2007), failing to heed Weber’s warning that such politically immature leaders will place other interest such as Malay nationalism (Heng 1997; Pepinsky 2007; Yacob & Khalid 2012).
above the goal of achieving enduring economic and political power for the nation through commercial success of its businesses. This developmental state model adopted by Malaysia’s ruling political powers will be expected to strongly influence external governance by legal and regulatory institution and internal governance by normative institutions such as GLCs.

Ethical Behaviour

Ethical behavior is behavior rooted in morals and obligations. It refers to the appropriate ways to pursue organization goals and objectives (Scott 2001) in accordance with socially determined behavior expectations rooted in morals and obligations (Alexander 2012). According to Woods and Lamont (2011), existing research ascribe many meanings to ethics depending on one’s philosophical perspective. However, guided by Schwartz’s (2002) universal moral standards of behavior, components of honesty, trustworthiness, justice and fairness, will also be expected to be standards of moral or ethical behaviour for the diverse cultures and diverse religions that make up Malaysian business organizations’ workforce.

External Governance

External governance by legal and regulatory institutions has 4 components. These include, laws and regulations as reference standards of behavior, monitoring adherence to these laws and regulations through audit and compliance, regulatory enforcement actions in the event of non-compliance to these laws and regulations and effectiveness of these laws and regulations in fostering competitive market behaviours. These components were ascertained from the in-depth interviews conducted with regulators during this research.

Laws and Regulations

The first component of external governance, laws and regulations constituting legal and regulatory institutions are essential and are well developed (Levine and Zervos 1998). A developing nation like Malaysia, with common law legacy (La Porta et al. 1998) will be expected to have written laws and regulations to safeguard investors from unethical behavior of businesses in market place.
Audit

The second component of external governance refers to monitoring role of audit firms and audit committees answerable to Board of Directors as required by legal and regulatory institutions. Audit firms are institutions that play role of fostering norms of accurate financial reporting behavior especially with respect to reducing earnings management (Lin and Hwang 2010). Lin and Hwang’s (2010) meta-analysis found that audit quality, auditor tenure, auditor size and specialization have a negative relationship with earnings management and that auditor independence as measured by audit fee and total fee ratio deters earnings management. However, there exist an apparent conflict of interests inherent in auditing companies. Audit companies are also paid directly for non-audit services by firms they audit and non-audit business is a repeat business and hence lucrative for audit firms to maintain good relationships. Though best practice call for disclosure of conflict of interest as a regulatory requirement (Jamal et al. 2016), Malaysian Stock Market listing rules do not require disclosure of non-audit services provided by external auditors (Abdul Wahab et al. 2014) which can represent a potential conflict of interest. Lin and Hwang’s (2010) meta-analysis also found that independence of Board of Directors and its expertise have a negative relationship with earnings management and that Board’s audit committee’s independence, size, expertise and number of meetings also have a negative relationship with earnings management. Notwithstanding these shortcomings, accurate financial reports certified by external auditors and the audit committee that reports to Board of Directors (BOD) will be expected to monitor compliance to laws and regulations and in so doing foster ethical behavior.

Regulatory Enforcement

The third component of external governance refers to motivating role of enforcement agencies mandated by legal and regulatory institutions to punish non-compliance to laws and regulations. Myrdal pointed out that the difficulty of formal institutions in shaping attitude is partly due to attitudes and institutions being inert and partly due to policies that aim to reform attitudes and institutions are themselves part of the unequal power and property structure of existing social system (Streeten 1990). In Malaysia, legal and regulatory institutions, through patronage, is run by people aligned to championing Malay economic and political interests of ruling
Malay party (Siddiquee 2010; Case 2001; Case 2005; Gomez and Jomo 1999:27; Teh 2002; Crouch 1996; Myerson 2008). Myrdal warns that legal and regulatory institutions themselves can be influenced by such political valuations of these cultural-cognitive institutions. Consequently, technocrats who administer these regulatory institutions have the tendency to neglect societal needs and bow to these vested interests (Streeten 1990). This is supported by a recent study where UK business elites were willing to use their influence over legal and regulatory institutions to deviate from best corporate governance practices to neutralize institutional change (Haxhi et al. 2013). In Malaysia, regulatory institutions act mainly according to political interests of ruling Malay party of favouring Malay ethnicity (Heng 1997; Pepinsky 2007; Yacob & Khalid 2012) rather than raison d’etre of public interest in the spirit of neutrality and fairness to all Malaysians. This results in their sanctioning being selective in the event of infringement of relevant regulations (Case 2008; Siddiquee 2010) which continues in the case of Government investment firm, 1MDB, which only suffered fines locally, whilst US Department of Justice have embarked on civil suit to recover assets worth US1billion purchased with money laundered from 1MDB (Wall Street Journal, 2016).

More importantly, the assumption that regulations will protect interest of public was challenged in 1971 by Stigler (1971). Stigler pointed out that regulations are routinely and predictably ‘captured’ and manipulated to serve interest of those who are supposed to be constraint by it- industries, professions and businesses- or to serve other special interest groups or to serve regulators themselves- bureaucrats and legislators- who write them or control their administration (Etzioni 2009). However, as Malaysia has reasonably well-developed institutional setting in terms of structure and potential enforcement authority (Siddiquee 2010), regulatory enforcement agencies will be expected to be immune to regulatory capture and hence positively impact ethical behaviour.

Competitive Market Behaviour

The fourth component of external governance is effective behavior change mechanism which can be determined by the level of competition among businesses. In Malaysia, State supported Malay dominated GLCs and State Economic Development Corporations (SEDC) were created by the New Economic Policy (NEP)
between 1970 and 1990. They did not arise according to their much lower costs of transactions compared to corresponding market costs but rather through ethnic Malay preferential opportunities of NEP which virtually provided them exclusive government projects and procurement contracts without need to compete for them in the market (Gomez and Jomo 1999; Perkins and Woo 2000; Heng 1997; Uddin & Uddin 2012; Yacob and Khalid 2012). Consequently, these firms will find such normally high transaction costs alluded to by Coase (Sampson 2003) associated with searching for suitable trading partners, acquiring information about what is on offer, appropriate terms to offer including negotiating contract and monitoring its fulfillment relatively much cheaper than in case of private Malaysian business firms.

Similarly, many of these GLCs grew to huge size not in accordance with reduced transaction cost relative to that of market as alluded to by Coase (Sampson 2003) but because of State’s Malay affirmative action NEP that favoured Malay managed firms over non-Malay managed firms (Gomez and Jomo, 1999; Perkins and Woo 2000; Heng 1997; Uddin & Uddin 2012; Yacob & Khalid 2012). Furthermore, the New Economic Model (NEM) that replaced the NEP aims to transform Malaysia into a high-income nation through focus on innovative processes, cutting edge-technologies, reliance on skilled talent and high-value operations primarily through the private sector and FDI (NEAC 2010). With NEM’s emphasis on private sector, FDI rather than GLCs and with the enactment of Competition Act in 2010 in Malaysia, businesses will be expected to base their market behaviours on creating innovative value adding products and services that are superior to what is offered by competitors.

Taken together, these components of external governances lead to the following hypothesis.

H1 External governance positively affects ethical behavior.

Internal Governance

Internal governance refers to governance/self-regulation exercised by each and every employee of an organization to foster ethical behavior. Carver and Scheier’s (1998) four components of self-regulation for individual behavior represent the components of internal governance exercised by employees. Firstly, presence
of a clear set of standards for employees to pursue or to preserve. More importantly, these should be organized in order of priority to permit effective conflict management amongst them (Fitzsimmons & Bargh 2004) when making decisions. Secondly, it requires employees to monitor for discrepancies between behavior of organization’s employees and these standards. Thirdly, it requires sufficient motivation to change behaviour of employees to adhere to these standards. Finally, it requires an effective mechanisms for employees’ behavioural change (Schmeichel & Braumeister 2004) to voluntarily comply with these standards.

Core Values

Ethics based core values, constituting the first component of internal governances’ standards of reference includes universal values such as honesty, trustworthiness, justice and fairness (Schwartz 2003). Individual employees in organizations are not mere robots who blindly follow organization performance goals and core values set by their leaders/superiors but are rational thinking beings who can decide for themselves. This individuality of employees has been supported by research on work values (Williams 2011), employee integrity (Chtioui and Dubuisson 2011) and personal values at work (Weaver and Trevino 1999). These employees have a critical stake in sustaining viability of organization for long term as their livelihood depends on it, similar to Ostrom’s (2010) research on sustainable management of common resource pool by communities even in the absence or weakness of legal and regulatory institutions. The presence of ethics based core values will provide a guiding standard for desired ethical behavior.

Feedback System

Feedback system on ethical issues, the second component of internal governance, refers to a monitoring system that captures employees’ feedback on ethical issues for managers of organization to act on. Organizations’ leaders and managers regularly monitor progress towards achievement of their growth and profit goals through their employees’ feedback of corresponding key performance indicators. The review of these and subsequent corrective actions or changes to refocus on goal achievement premised on ethical values will collectively represent a good feedback system that influences ethical behaviour. Such integrity based programs have been associated with employee willingness to report misconduct, employee commitment to firm, that it is acceptable
belief on part of employee to submit 'bad news' to management and belief that they can live by their personal values at work (Weaver and Trevino 1999). To date, there is still insufficient research to show effectiveness of feedback system on resolving ethical issues before they worsen. However, the presence of such monitoring system will be expected to impact ethical behavior positively.

Performance System

Ethics based Performance System, the third component of internal governance, provides motivation to comply with core values of organization. Virtually all organizations have in place a performance system. A performance system is one that focuses all employees on achieving common organization goals especially profit and growth. An ethics based performance system, is a motivator that focuses on goal achievement premised on doing so ethically (Alexander 2012) that is honestly, fostering trust, justly and fairly. Profit-oriented organizations ensure that their performance system aligned to goals of organization by being incentivized or motivated according to Myerson’s Mechanism Design Theory (2008). This is not so with government regulatory bodies and government development and procurement entities in general leading to them seeking incentives by other unethical means such as through corruption and bribery as is evident by 2014 Transparency International report, where Malaysia obtained a poor rating of 52 out of 100 (Malaysian Insider Online 2014c).

It will not be surprising that in most profit oriented organizations, predominant performance culture will be linked to reward/remuneration and career progression systems. The latter will incentivize its employees to focus on a culture of performing and achieving organization key performance indicators (KPI) which are linked to organization revenue growth and profitability goals in accordance with Myerson’s (2008) mechanism design theory. However, business organizations are expected to achieve their organization goals and objectives in appropriate way (Scott 2001) in accordance with socially determined behavior expectations rooted in morals and obligations (Alexander 2012). Hence ethics-based performance system will be expected to positively impact ethical behavior.
Corporate Governance

Corporate Governance behavior of employees, the fourth component of internal governance, will reflect effective behavior change mechanism in relation to core values being internalized by employees and practiced in their work. According to Mcdonald (2009) organization code of conduct can be easily eroded (and enhanced) given attitude and behaviours of supervisors and organizational leaders. Hence presence of a code of conduct by itself does not translate into an ethical organization. It is a document which needs leaders to breathe life into it by practicing its precepts, failing which, it is a mere lifeless document (Mcdonald 2009). Alternatively, an integrity based approach will focus on establishing legitimacy with employees through internally developed organizational values/core values and self-governance-through inspiring employees to live up to company's ethical ideals (Brien 1996). Weaver and Trevino (1999) found that whilst compliance program had positive impact, employees aware of ethical issues, were willing to seek advice, helped in decision making and reduced observable unethical behavior, such program seen as integrity based were a stronger predictor of these outcomes. Trevino and Youngblood (1990) found that a value-based cultural approach was most effective in preventing ethical lapses of behaviour. It is expected that organization’s corporate governance premised on ethical core values will lead to ethical behavior of employees in the workplace.

Taken together, these components of internal governance help us arrive at the following hypothesis.

**H2** Internal governance positively affects ethical behaviour.

**Development of an Integrative Governance Model**

As Weber (1984) pointed out, economic policies of State must serve power political interest of nation whether through direct intervention in economic life or freeing economic forces of nation for their autonomous development. In Malaysia, cultural-cognitive institutions of the ruling government will be expected to influence legal and regulatory institutions’ external governance role through New Economic Model (NEM) policies and directly influence normative institutions’ internal governance through direct intervention in market place through GLCs (Heng 1997; Pepinsky 2007; Stafford 1997; Yacob & Khalid 2012; Uddin & Uddin 2012).
Consequently, ethical behavior of GLCs in market place will be accordingly impacted. Accordingly, a model of governance in figure 1 is proposed, encompassing 3 pillars of institutional theory namely legal-regulatory, cultural-cognitive and normative. External governance components includes laws and regulations, auditors that monitor compliance to laws and regulations, regulatory enforcement of laws and regulations and competitive market behavior of business organizations that reflect the spirit of adherence to laws and regulations. Internal governance components includes ethics based core values, feedback monitoring system of compliance to core values, performance system motivation to comply with core values and corporate governance behavior of organization’s employees that reflect core values.

![Integrative Governance Model](image)

**Figure 1**

Integrative Governance Model

**Methodology**

Data Collection Method

Data was collected in two phases. In the first phase, stretching from May 2015 to October 2015, in-depth interviews were conducted with top management of key regulators and GLCs constituting top 100 companies listed in Malaysian Stock Market (Bursa Saham Malaysia). 8 GLCs and 7 legal and regulatory institutions volunteered to be interviewed. These included Central Bank (Bank Negara Malaysia), Malaysian Anti-
Corruption Agency (MACC), Malaysian Stock Market (Bursa Saham Malaysia), Malaysian Institute of Corporate Governance, Companies Commission of Malaysia and National Integrity Institute. Semi-structured questions were used and provided in Appendix A. Profile of interview respondents is given in table 2.

Table 2 Profile of Interview respondents

<table>
<thead>
<tr>
<th>Interviewee code</th>
<th>Organization type</th>
<th>Job position type</th>
<th>Gender</th>
<th>Age group</th>
<th>Ethnic group</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Regulatory</td>
<td>Deputy CEO/Management</td>
<td>Male</td>
<td>51-60 years</td>
<td>Malay</td>
</tr>
<tr>
<td>B</td>
<td>Regulatory</td>
<td>Deputy CEO/Management</td>
<td>Male</td>
<td>41-50 years</td>
<td>Malay</td>
</tr>
<tr>
<td>C</td>
<td>Regulatory</td>
<td>MD/CEO/Equivalent</td>
<td>Female</td>
<td>41-50 years</td>
<td>Others</td>
</tr>
<tr>
<td>D</td>
<td>Regulatory</td>
<td>Deputy CEO/Management</td>
<td>Male</td>
<td>51-60 years</td>
<td>Malay</td>
</tr>
<tr>
<td>E</td>
<td>Regulatory</td>
<td>Deputy CEO/Management</td>
<td>Female</td>
<td>41-50 years</td>
<td>Chinese</td>
</tr>
<tr>
<td>F</td>
<td>Regulatory</td>
<td>Deputy CEO/Management</td>
<td>Female</td>
<td>51-60 years</td>
<td>Chinese</td>
</tr>
<tr>
<td>G</td>
<td>Regulatory</td>
<td>MD/CEO/Equivalent</td>
<td>Male</td>
<td>51-60 years</td>
<td>Malay</td>
</tr>
<tr>
<td>GLC1</td>
<td>GLC</td>
<td>Deputy CEO/Management</td>
<td>Male</td>
<td>41-50 years</td>
<td>Malay</td>
</tr>
<tr>
<td>GLC2</td>
<td>GLC</td>
<td>Deputy CEO/Management</td>
<td>Female</td>
<td>41-50 years</td>
<td>Malay</td>
</tr>
<tr>
<td>GLC3</td>
<td>GLC</td>
<td>Deputy CEO/Management</td>
<td>Female</td>
<td>41-50 years</td>
<td>Malay</td>
</tr>
<tr>
<td>GLC4</td>
<td>GLC</td>
<td>Deputy CEO/Management</td>
<td>Male</td>
<td>41-50 years</td>
<td>Malay</td>
</tr>
<tr>
<td>GLC5</td>
<td>GLC</td>
<td>Deputy CEO/Management</td>
<td>Female</td>
<td>51-60 years</td>
<td>Chinese</td>
</tr>
<tr>
<td>GLC6</td>
<td>GLC</td>
<td>Other Top Management</td>
<td>Female</td>
<td>51-60 years</td>
<td>Malay</td>
</tr>
<tr>
<td>GLC7</td>
<td>GLC</td>
<td>MD/CEO/Equivalent</td>
<td>Male</td>
<td>41-50 years</td>
<td>Malay</td>
</tr>
<tr>
<td>GLC8</td>
<td>GLC</td>
<td>Deputy CEO/Management</td>
<td>Female</td>
<td>41-50 years</td>
<td>Malay</td>
</tr>
</tbody>
</table>

In the second phase, a survey using a structured questionnaire was conducted on selected GLCs. 113 responses were successfully obtained which is well beyond minimum sample size of 68 calculated by Gpower 3.1 using power of 0.8. Common method variance bias was reduced through procedural remedies including ensuring participant anonymity and confidentiality, randomizing survey questions, using clearly written and precise scale items, informing participants of the need for honest responses, providing and providing context, purpose of survey, appropriate motivation to complete the survey, providing clear instructions for questionnaire completion and avoiding complicated wording and syntax (Podsakoff et al 2012). The survey questions are provided in Appendix B. A description of the survey respondents is given below.

Profile of survey respondents

The survey respondents were employees of GLC7 who volunteered to complete the survey without any compulsion on part of their organization management. They reflect diverse profile of employees in organization. In relation to job function, 41% were in technical or engineering function, 32% were in legal,
human resources and related services function, 6% were in sales and marketing function, 4% were in finance function and 3% were in production function. In terms of job position, 4% were senior managers or equivalent, 3% were department heads or equivalent, 11% were managers or equivalent and 70% were officers or equivalent. In terms of academic qualifications, 39% had postgraduate level qualification and 50% had degree level qualification. In terms of age group, 27% were between 21-30 years, 32% between 31-40 years, 24% between 41-50 years and 6% more than 50 years. In terms of ethnicity, 80% were of Malay ethnicity, 4% Chinese ethnicity and 3% Indian ethnicity.

Measures

The measures were determined from the interview phase with regulators in particular and top management of GLCs. The corresponding scales were taken from literature where available and the rest adapted from the interviews. These were pilot tested for validity and reliability. The measures for analyzing survey data is provided in table 1 below.

**Table 1 Measures**

<table>
<thead>
<tr>
<th>Construct</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Internal governance</strong></td>
<td></td>
</tr>
<tr>
<td>2. Feedback system</td>
<td>2. Weaver and Trevino (1999)*</td>
</tr>
<tr>
<td>3. Performance system</td>
<td>3. Schminke et. al. (2007)*</td>
</tr>
<tr>
<td><strong>External governance</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Ethical Behaviour</strong></td>
<td></td>
</tr>
</tbody>
</table>

Note: * Adapted and modified based on interviews with regulators and top management of GLCs.

Data Analysis
The in-depth interview data and open-ended question responses in survey data from GLC7 were analyzed using software Nvivo 10, which is a software for analyzing qualitative data to bring out emerging themes. The interviewees for GLC were labelled from GLC1 to GLC8 whilst the regulators interviewed were labeled from A to G. The survey data was analyzed using Partial Least Square (PLS) based Structural Equation Modeling (SEM), SMART PLS version 3.

Results

We start by presenting the PLS results of the measurement model including results for reliability and validity of survey data, which will then be followed by PLS results for structural models based on bootstrapping method (5000 resamples) to determine significance levels of loadings, weights and path coefficients. The latter will include the results of the final blindfolding step to give predictive relevance scores.

Content validity of survey questionnaire and interview questions was obtained through peer reviewed literature. Face validity was obtained through pretesting survey questionnaire and interview questions with relevant industry experienced individuals. Construct validity was obtained through use of relevant statistical validity constructs such as p-value or significance among others. In case of survey data, use of relevant statistics available in PLS 3 were used to assess reliability of survey data. Using PLS 3.0, the measurement model given in figure 2 was tested. The measurement model has both formative and reflective measures. The reflective measures were assessed using convergent validity and discriminant validity analyses. Factor loadings, Composite Reliability (CR) and Average Variance Extracted (AVE) were used to assess convergent validity. Most reflected item loadings exceeded recommended 0.5, as well as all CR and AVE values as shown in table 3, 4 and 5, exceeded recommended value of 0.7 and 0.5 respectively (Ringle et al. 2015). The ones that did not were progressively deleted. Complete survey questions are provided in Appendix B.
Figure 2 Measurement Model
<table>
<thead>
<tr>
<th>Statement</th>
<th>Question</th>
<th>Factor Loadings</th>
<th>Composite Reliability</th>
<th>Average Variance Extracted</th>
</tr>
</thead>
<tbody>
<tr>
<td>Feedback System</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Managers are concerned about unethical work issues</td>
<td>F1</td>
<td>0.83</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees openly discuss with managers unethical work issues</td>
<td>F2</td>
<td>0.86</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reports of unethical work issues investigated</td>
<td>F3</td>
<td>0.85</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees report unethical work behaviours</td>
<td>F4</td>
<td>0.77</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Performance System</td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Employees willing to break rule to advance careers</td>
<td>J11</td>
<td>0.79</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Personal success more important than helping others</td>
<td>J15</td>
<td>0.79</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees strive to obtain power and control</td>
<td>J16</td>
<td>0.74</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees willing to lie to advance careers</td>
<td>J17</td>
<td>0.84</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Corporate Governance</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees provide accurate work information</td>
<td>CG2</td>
<td>0.80</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees provide complete work information</td>
<td>CG3</td>
<td>0.79</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees provide objective work information</td>
<td>CG4</td>
<td>0.82</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees provide relevant work information</td>
<td>CG5</td>
<td>0.73</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees provide timely work information</td>
<td>CG6</td>
<td>0.81</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees comply with rules and regulations</td>
<td>CG7</td>
<td>0.77</td>
<td></td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Statement</th>
<th>Question</th>
<th>Factor Loadings</th>
<th>Composite Reliability</th>
<th>Average Variance Extracted</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Internal/external auditors act with integrity</td>
<td>B1</td>
<td>0.82</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Internal/external auditors are independent</td>
<td>B2</td>
<td>0.84</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Internal/external auditors identify areas to audit</td>
<td>B4</td>
<td>0.69</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Regulatory Enforcement</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Use good relationship with regulators when unable to follow laws</td>
<td>O1</td>
<td>0.80</td>
<td></td>
<td></td>
</tr>
<tr>
<td>When we do not follow regulations, authorities will not do anything</td>
<td>O3</td>
<td>0.72</td>
<td></td>
<td></td>
</tr>
<tr>
<td>When authorities want to take action, use our political connections</td>
<td>O5</td>
<td>0.81</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Competitive Market Behaviour</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compete with other companies</td>
<td>A1</td>
<td>0.71</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Appropriate terms to win business contracts</td>
<td>A3</td>
<td>0.79</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Create superior value</td>
<td>A7</td>
<td>0.74</td>
<td></td>
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Table 5 Loadings, CR and AVE for Ethical Behaviour

<table>
<thead>
<tr>
<th>Statement</th>
<th>Question</th>
<th>Factor Loadings</th>
<th>Composite Reliability</th>
<th>Average Variance Extracted</th>
</tr>
</thead>
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<tr>
<td>Ethical Behaviour</td>
<td></td>
<td>0.92</td>
<td>0.58</td>
<td></td>
</tr>
<tr>
<td>Employees conceal information from customers</td>
<td>K1</td>
<td>0.78</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees report seemingly better performance</td>
<td>K2</td>
<td>0.73</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees conceal performance information from superior</td>
<td>K3</td>
<td>0.78</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees do not tell complete truth to customers</td>
<td>K5</td>
<td>0.73</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees do not tell complete truth to auditors</td>
<td>K6</td>
<td>0.81</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees fail to inform customers of important changes</td>
<td>K7</td>
<td>0.72</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees do not tell complete truth to superior</td>
<td>K8</td>
<td>0.79</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Employees withhold damaging information from customer</td>
<td>K9</td>
<td>0.76</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Discriminant validity was then tested for all constructs and Heterotrait-Monotrait ratios were all found to be less than recommended 0.9 (Ringle et al. 2015). These results indicate that there was no problem with discriminant validity amongst constructs. In order to validate formative measures, multicollinearity between indicators were tested by determining variance Inflation Factor (VIF). We used a stricter measure for VIF and found that all VIF were less than 5.

This was followed by bootstrapping method (5000 resamples) to determine significance levels of loadings, weights and path coefficients of structural model (Ringle et al. 2015). The final blindfolding step was used to give predictive relevance $Q^2$ scores (Ringle et al. 2015). Table 6 gives summary of structural model.

Table 6 Summary of Structural Model

<table>
<thead>
<tr>
<th>Hypothesis</th>
<th>Relationship</th>
<th>Standard Beta</th>
<th>Standard Error</th>
<th>T Value</th>
<th>Decision</th>
<th>$R^2$</th>
<th>$f^2$</th>
<th>$Q^2$</th>
</tr>
</thead>
<tbody>
<tr>
<td>H1</td>
<td>External Governance $\rightarrow$ Ethical behaviour</td>
<td>-0.27</td>
<td>0.12</td>
<td>2.26</td>
<td>Supported**</td>
<td>0.15</td>
<td>0.05</td>
<td>0.08</td>
</tr>
<tr>
<td>H2</td>
<td>Internal Governance $\rightarrow$ Ethical behaviour</td>
<td>-0.14</td>
<td>0.14</td>
<td>0.99</td>
<td>Not Supported</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

** $p$-value $< 0.05$
Only one of the hypotheses was supported namely external governance positively affects ethical behavior. As $Q^2 > 0$, model has good predictive relevance. The corresponding effect size $f^2$ is considered small based on Cohen (1988).

The key themes that emerged from interviews with top management regulators, GLCs and from open-ended question responses from 113 survey participants of a GLC will be discussed in next section.

**Discussion**

The main purpose of this research is to promote ethical behavior by making the case for adopting internal governance by business organizations to complement external governance by legal and regulatory institutions. The quantitative analysis found that external governance positively affects ethical behavior. In this section, qualitative findings will be discussed to show that external governance in a developing nation like Malaysia is weakened by many factors other than ones identified by literature and internal governance is not supported since it is not emphasized by business organization as well as not actively endorsed by regulators. More importantly, key stakeholders, the employees of business organizations, have the potential, if organizations actively adopt internal governance, to foster ethical behavior at a much lower cost than current costly compliance regiment espoused by legal and regulatory institutions worldwide that may be also be retarding economic growth and development.

**External Governance**

From qualitative analysis, it will be shown that external governance is not fully effective and evidence will be presented in relation to the 4 components of external governance namely laws and regulations, auditors that monitor compliance to laws and regulations, regulatory enforcement of laws and regulations and competitive market behavior of business organizations that reflect spirit of adherence to laws and regulations.

The changes to laws are trending towards increasing complexity which makes understanding non-compliance in relation to ethical behavior even more difficult. According to regulator F and GLC3, laws and regulations are becoming more complex and are often changing with changes in business environment.
Complexity also arises from adopting external global standards that appear too high especially for relatively newer Malay managed GLCs compared to well established MNCs according to GLC1.

“BOD being more firm with organization on this matter. But being director is very taxing and non executives directors need to keep pace with all regulatory changes… But rules are internationally driven. Major challenge: capacity to implement the rule, understanding the rules. Example capital doc 900 pages. Accounting rules complex. Own supervisors and regulators can understand. But rules when they are ready need to avoid unintended consequences.”.-F

The monitoring of compliance to laws and regulation by auditors is made difficult by detrimental impact of costly compliance regiment on potential higher investments generation of profits, lack of compliance expertise which delays audits and existence of conflicts of interests. According to GLC1, reduction of profits experienced by GLCs is attributed to costly and time consuming compliance systems that needs to be put in place.

You need to have revenue of billion ringgit since very costly to maintain full time secretarial team. Instead of doing more productive work, they are spending time releasing info. I am all for transparency. But Bursa needs to be clever not to stifle the market. Competition needs some grey areas…”… (Complying with regulations) is costly in terms of resources and time. Time is money and (this compliance) takes away focus from business. Before do anything (like complying with Bursa) need to be in business to make money”.-”-GLC1

Furthermore, according to GLC3, legal and regulatory requirement for internal auditors or compliance staff monitoring compliance are made worse by latter’s lack of auditing/compliance competency and consequent adoption of simplistic ‘box-ticking’ approach to auditing. This finding is in contrasts to Lin and Hwang’s (2010) meta-analysis presumption that auditor competence is a given precondition for enhancing audit quality to deter unethical earnings management behaviour. According to regulator G, this lack of competency leads to delays in certifying financial accounts by external auditors. Furthermore, regulator G identifies a primary reason for such delays which has been of common occurrence in Malaysia over past 6-7 years as due “to especially big loss or suspicious payment to parties or to strange companies which rarely do business with and with no supporting documents”. Furthermore, though best practice call for disclosure of conflict of interest as a regulatory
requirement (Jamal et al. 2016), Malaysian Stock Market listing rules do not require disclosure of non-audit services provided by external auditors (Abdul Wahab et al. 2014), a common practice in Malaysia, which can represent a potential conflict of interest. In the absence of disclosure of conflicts of interests, it is an exercise in futility to make calls for improving external auditor performance quality by setting clear rules for auditor work performance as espoused by SEC’s Chief Accountant, James Schnurr (Wall Street Journal 2014d).

The legal and regulatory requirement for GLC’s BOD especially through their audit committees to play an oversight role on business organization’s management team decisions is virtually non-existent due BOD’s lack of functional competency. According to regulator G and GLC1, BOD’s lack functional competency as they primarily hail from non-profit oriented state ministries with untested business acumen.

“Practice of company directors in Malaysia are appointed from Senior ex retirees of government Ministries. What is their education background, career and what area of industry? … probably they are good administrators and (experience is) different from (guiding) business companies and they now land in company, in dog eat dog world”.G

This is contrary to best practice requirements of independence and expertise of Board of Directors as identified by Lin and Hwang’s (2010) meta-analysis to deter unethical earnings management behaviour. Consequently, it is not surprising that 33% of GLC survey respondents also identify lack of professional competency as reason for occurrence of unethical behaviours in organizations.

Extent literature contents that regulatory enforcement is weak primarily due to regulatory capture (Stigler 1971; Etzioni 2009) and that regulatory institutions act mainly according to political interests of ruling Malay party of favouring Malay economic interest (Heng 1997; Pepinsky 2007; Yacob & Khalid 2012) of GLCs that leads to sanctioning being selective in event of infringement of relevant regulations (Case 2008; Siddiquee 2010). Our findings indicate that it is also due to lack of enforcement competency on the part of regulatory enforcement institutions, lack of coordination amongst these enforcement institutions and the ineffectiveness of fines imposed for non-compliance. According to GLC3 and regulator D, legal and regulatory enforcement agencies are limited by serious lack of coordination among enforcement agencies as well as unqualified enforcement officers respectively.
“Regulations do not facilitate enough coordination among regulatory agencies. Sorely lacking due to function of politics where do not want to step on each others toes, turf mentality. Secondly, implementation is always a problem since do not think things through to the end… “

GLC3

These enforcement limitations are made worse when the State subordinates the Whistle-blower Act to the Official Secrets Act and Banking and Financial Services Act (Malaysian Insider Online 2015e) to protect unethical financial behavior as epitomized in the case of the GLC, 1MDB (Wall Street Journal 2015f). It has been contented by Siddiquee (2010) that Malaysia has reasonably well-developed institutional setting in terms of structure and potential enforcement authority and presumably imposition of fines for non-compliance will deter unethical business behavior. However, our findings indicate otherwise. According to regulator B, the common enforcement practice of imposing fines is not a deterrent. Deputy Governor of Bank of England, Minouche Shafik, pointed to the real risk of errant business firms treating fines as a mere acceptable cost of doing business (Wall Street Journal 2015a).

The Competition Act 2010 with its primary purpose of protecting consumers (See 2015) through fostering competitive market behaviours rather than non-competitive rent seeking or collusive behavior, entails adopting a competitive mindset which is not evident in Malaysia despite 5 years of passage of Competition Act. Rent seeking behavior continues under New Economic Policy’s current variant of New Economic Model (Ariff 2012) which provides GLCs exclusive access to government projects and procurement contracts without the need to compete for them in the market (Heng 1997; Pepinsky 2007; Yacob & Khalid 2012). According to GLC7, Competition Act is inconsistently applied in Malaysia where there is still a restriction in issuing licenses to compete even with dominant primarily GLC players. In addition, according to GLC3 there is belief that the Act does not apply to GLCs. It is not surprising then that rent seeking predominates especially for GLCs, who view competitive market behavior as in distant future with no need to prepare for its imminent reality. As GLC7 CEO aptly put it:

“I expect even with TPPA (Trans Pacific Partnership Agreement), it will be (foreign) MNCs competing with (local Malaysian) Chinese firms mainly. GLCs will not be affected. I see foreign firms tying up with local GLC firms (as current practice)
to bid for government projects” and “the GLCs and (Malaysian) Chinese companies do not cross into each other’s markets.”– GLC7

In Malaysia, Competition Act 2010 also serves the purpose of promoting economic development through competition among business entities (See 2015) to fosters innovation driven generation of globally competitive superior products and services for consumers worldwide. However, according to GLC1, GLCs do not feel the need to acquire functional competency to innovate and only need to capitalize on existing technology. The competitive mindset is also absent from GLCs’ majority shareholders, ruling State, which has been in power since 1957, explains similar attitude of its GLCs, in general. The absence of this competitive mindset becomes obvious in Malaysia, where one sees that the ruling political party has increasingly resorted to winning election campaigns with unethical vote buying behaviour (Wall Street Journal 2016e) rather than serving electorate through superior governance abilities in comparison to opposition parties.

Internal Governance

It is not surprising that our findings from the survey analysis points to internal governance’s effect on ethical behavior not being supported. This will be explained by the qualitative analysis, where, it will be shown that internal governance is not emphasized by the GLC organization that was surveyed. The evidence will be presented in relation to the 4 components of internal governance namely ethics based core values, feedback monitoring system of compliance to core values, performance system motivation to comply with core values and corporate governance behavior of organization’s employees that reflect core values. Furthermore, it will be shown that these components of internal governance is clearly seen by employees as important for fostering organization wide culture of ethical behavior as more effective than a mere “tone from the top” as espoused by regulators. Consequently, if they are strengthened and empowered, employees as a community have the potential to govern their ‘common resource pool’ namely sustainability of their business organization through actively fostering a culture of ethical business behaviours throughout every aspect of their organization in accordance with Ostrom’s (2010) findings on community based governance.
The survey respondents clearly espouse the adoption of ethics-based core values such as professionalism, honesty and trustworthiness as a basis for ethical behavior in contrast to current legal and regulatory espousal of the tone from top management. On the contrary, our findings indicate that management emphasizes loyalty. According to regulator D, in relation to standards, organization core values of GLCs primarily emphasize loyalty rather than professionalism based on ethics/universal moral standards as espoused by Schwartz (2002) and Trevino and Youngblood (1990). Loyalty of GLC to its majority shareholder, ruling State, becomes clear when GLC7 supported the Malaysian Prime Minister’s call to GLCs to bring back US$100 Bil money back to Malaysia from their overseas investments by saying, “Malaysian GLCs need to do national service.” This ethics deficiency of GLCs is evident when GLC3 pointed out that ethics based principles as core values are incompatible with business and are not discussed in their organization. This is confirmed by Regulator D:

“Feel very heavy since if trying to do business strictly by following principle of integrity maybe they feel quite difficult if need to comply with integrity values. Business sector running differently but government also trying to follow private sector”... Honesty is something personal and not related to money or profit. After 30 years in government this is their mindset.” D

This absence of ethical tone from the top is clearly seen by the employees where, GLC survey respondents point to inadequate professional competency (33%), conflict of interest (24%) and dishonesty (14%) as primary reasons for unethical behavior observed in their organization. Hence, without explicit ethics based principles such as honesty, trustworthiness and professionalism as part of core values governing employee behaviour, employees lack the guiding principle in performing their jobs.

In relation to monitoring adherence to core values, which to date has not been well researched, our findings indicate that this is an important component from survey respondents’ viewpoint that has been neglected by management for fostering ethical behavior. The GLC survey respondents (10%) point to monitoring of unethical behaviours by GLC employees as being weak. Though only 18% of survey respondents advocate monitoring of unethical behavior as important for better internal governance, the small number is more a reflection of ethical standards not being explicit in core values as well as loyalty being the predominant
value emphasized by their GLC top management and majority shareholder, the State. Regulator A also supports this need for organization to emphasize monitoring compliance.

“Stress on monitoring must come from within organization ... Cannot expect regulator A to go in ... it must come from within organizations. Regulator A when receive info will take action: carry out investigation and look into system and procedures and if contradict any legislation.”-A

Though Weaver and Trevino (1999) point to integrity based programs being associated with employee willingness to report misconduct, it will fail if ethical values are not an explicit part of organization core values and if the organization fails to get all their employees to monitor adherence to these values to foster ethical behaviour.

Business organizations are expected to achieve their organization goals and objectives in appropriate way (Scott 2001) in accordance with socially determined behavior expectations rooted in morals and obligations (Alexander 2012) or other higher order values or ethical principles as pointed out by Greenwood et al. (2010). However, our findings indicate that achievement of organization goals are rooted primarily on profits.

“KPI on control function of compliance officers should not be driven by business indices since put them on conflicted lines.”-F

This is not surprising when organizations incentivize its employees to focus on achieving organization revenue growth and profitability goals in accordance with Myerson’s (2008) mechanism design theory. According to regulator F, in relation to motivation to adhere to standards, achieving profits is the most important motivator. Furthermore, in the event of infringement of organization standards of behaviour, 29% of GLC survey respondents point to poor enforcement as unethical work behaviours are not punished or lightly punished or even condoned. Regulator B was emphatic in saying that Malaysians are not afraid of enforcement. It is revealing to note that motivation to work is generally lacking in the light of the finding that 22% of GLC survey respondents point to the lack of job motivation as a cause of unethical behaviours within GLC. This may be attributed to GLCs having captive business with no obvious competitor, negating the need to motivate
employees to focus on enhancing competitiveness through creativity, efficiency, productivity and effectiveness behaviours.

It was Brien’s (1996) work which emphasized the need for an integrity based approach focused on establishing legitimacy with employees through internally developed organizational values/core values and self-governance-through inspiring employees to live up to company’s ethical ideals. This is contrary to our findings which indicate that in relation to effective behavior change mechanism, top management of regulators and GLC heads surprisingly see no potential active roles that employees can play in curbing unethical behaviours. This could be due to the prevailing paradigm that only legal and regulatory institutions can influence effective behavior change as epitomized by the Dodd-Frank Wall-Street Reform and Consumer Protection Act (Smith and Muniz-Fraticelli 2013). However this narrow viewpoint is not shared by key stakeholders namely employees of organization who see organization as their ‘common’ resource pool that supports their livelihoods. GLC survey respondents attribute the lack of effective behavior change (25%) as a cause of unethical behaviours and the need to focus on this aspect of governance (27%) as a remedy. Consequently, there is a need to revive corporate governance beyond the BOD level as espoused by legal and regulatory institutions to encompass corporate governance practices by all employees to create an organization wide culture of ethical behaviour as evident by Trevino and Youngblood’s (1990) research which found that a value-based cultural approach was most effective in preventing ethical behavioural lapses.

Overall, it is clear that GLCs are unable to play their internal governance role primarily because its leaders and regulators do not see a need for it to be emphasized in their organization. However, this view is beginning to change with the 2015 UK’s Fair and Effective Market Review Report. According to the Report, two underlying principles needed to improve business conduct are the need for employees to be accountable for their actions/conduct and for business firms to take greater steps to improve standards of business practices (Wall Street Journal 2015a). These principles of collective responsibility of all employees and the adoption of ethics based business values as core organization values mirrors our findings for reviving internal governance role of business organizations like GLCs to complement external governance by legal and regulatory institutions. This would entail incorporating higher order values such as honesty, fairness, trustworthiness and
professionalism as part of organization core values. With these ethical core values in place, businesses like GLCs can achieve their goals and objectives ethically in compliance with relevant laws and regulations. Furthermore, motivating employees with strict enforcement for infringements as well as critically, providing them capabilities to perform their jobs ably without the need to resort to fraudulent practices such as dishonesty and conflicts of interests to achieve their job objectives are equally important. When all employees irrespective of rank or status are monitored for adherence to these ethical standards and prompt enforcement taken for infringements, then it is possible for all employees to be role models of exemplary behavior. This is consistent with bottom up community rule-formation and enforcement as uncovered by Ostrom’s work on common resource pool (Earl and Potts 2011). This employee community role is especially important where legal and regulatory institutions are generally weak and regulators, according to Regulator F, continue to make futile calls for ethical leadership especially for GLCs in accordance with the prevailing paradigm for ethical role model of business leaders (Frisch & Huppenbauer 2014).

Finally, a Weberian developmental state model is needed for internal governance and external governance to foster ethical business behavior especially as GLCs continue to serve the political goal of incumbency (Lopez 2012) rather than being competitive regionally and globally. In fact, since 2000, Malaysia has been slow in industrial upgrading (Rasiah 2012) indicating, a lack of emphasis on constantly recreating competitive advantage expected of normal private business entities. An even better solution is for the State to exit direct involvement in running businesses through rapid divestments of GLCs. This is supported by the 2013 Asian Development Bank (ADB) report, titled “Are GLCs crowding out private investment in Malaysia?”, affirming their findings that “when GLCs are dominant in an industry, investment by private firms is significantly negatively impacted ... To revive private investment... government must not only redress its growing fiscal deficit, but also expedite its programme of divestment” (Malaysian Insider 2015e). In this context, the Malaysian State of Penang, illustrates this Weberian developmental state model of mature political leadership. Penang State government has shown remarkable achievements when it followed adage that “the business of government is not to get into business” but to create an entrepreneurial state. Speaking at Merton College Oxford University in 2015, Chief Minister of Penang pointed out that its investment led, inclusive and sustainable wealth creation initiatives resulted in Penang State’s
projection to achieve 6.2% growth in 2015, achieved $11 billion (RM48 billion) investments since governing state in 2008, achieved a very low 1.2% unemployment rate despite net migration, expected GDP per capita income of $10K (RM40K) and a 11% reduction in Gini coefficient to 0.37 compared to the 2012 national average of 0.42 (Malaysian Insider Online 2015g).

Implications and Conclusion

Clearly, legal and regulatory institutions are not fully competent and fully independent to foster effective governance role on normative institutions such as GLCs, as they are primarily influenced by cultural-cognitive ruling government institutions based on non-Weberian developmental state model. In addition, GLCs do not have in place effective internal governance mechanism that has zero tolerance for unethical behaviours primarily because internal governance is not seen as important by either regulators or head of GLCs.

This research has advanced literature by proposing an Integrative Governance Model that incorporates both internal governance and external governance, for understanding ethical behavior. Then from a managerial perspective, business organizations can do more to complement external governance by reviving internal governance mechanism through incorporating ethical values as higher order values than profit, putting in place effective monitoring and motivating systems tied to adherence to ethics in business conduct, enforcing strictly infringements and practicing corporate governance by all employees. The State also needs to adopt Weberian development state model of mature political leadership by accelerating transformation of GLCs including privatizing them and consistently applying the Competition Act 2010 to help all Malaysian businesses to be globally competitive. Finally, to effectively combat unethical behaviours, legal and regulatory institutions need to exert their independence to act without fear or favour by emphasizing their own internal governance.

A limitation of the research is that the survey was conducted on only 1 GLC. In future, it would be good to conduct the research over more GLCs as well as private businesses and multinational companies operating in Malaysia to confirm the broad need to adopt internal governance to complement external governance rather than the current paradigm of exclusive, costly, growth and profit sapping external governance as a panacea for unethical business behaviours.
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Appendix A

Interview Questions

<table>
<thead>
<tr>
<th>Item no</th>
<th>Questions</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>Interviewer introduction and purpose of research project in relation to policy advise (5 min)</td>
</tr>
<tr>
<td>1</td>
<td>What are the 3 most common non-compliances committed by business organizations that you regulate? (5 min)</td>
</tr>
<tr>
<td>2</td>
<td>What are the 3 most common reasons for these non-compliances? (5 min)</td>
</tr>
<tr>
<td>3</td>
<td>What are the 3 most important steps business organizations can take to reduce such non-compliances? (5 min)</td>
</tr>
<tr>
<td>4</td>
<td>What are the challenges you are currently facing in relation to the following? (20 min): 1. regulatory rule changes 2. monitoring business organization’s compliance to regulations 3. encourage and assist business organizations to comply with regulations 4. Helping organizations develop ethical values amongst their employees</td>
</tr>
<tr>
<td>5</td>
<td>What specific assistance would you need from other institutions/Bodies (board of directors, external auditors and/or Parliament) to help you overcome these challenges? (10 min) a. BOD b. External Auditors c. Government/Parliament d. others (NGOs)</td>
</tr>
<tr>
<td>6</td>
<td>What more can business organizations you regulate do in terms of the following(10 min) 1. incorporate awareness on relevant regulations in their employees 2. monitor their employees’ compliance with relevant regulations 3. motivate their employees to comply with relevant regulations 4. Help in developing ethical values amongst their employees</td>
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Appendix B

Survey Questions

Audit. (Monitoring)

B1. During audit, internal/external auditors act with integrity and objectivity.

B2. During audit, internal/external auditors are independent in performing audit.

B3. During audit, internal/external auditors resist pressure by the company managers to ignore non-compliance issues.

B4. During audit, internal/external auditors independently identify areas to audit.

B5. During audit, internal/external auditors are seen as trying to uncover weaknesses in work processes in order to reduce non-compliance or abuses of power.

Regulatory Enforcement (Motivation)

O1. In this company, we use the good relationship with the regulators when unable to follow laws and regulations.

O2. In this company, when regulations are difficult to follow, we use other ways to do the business.

O3. In this company, when we do not follow regulations, the authorities will not do anything.

O4. In this company, when we do not follow regulations, we ask the authorities for more time.

O5. In this company, when authorities want to take action for not following regulations, we use the political connections/personal relationship to protect us.

Competitive Market Behaviour. (Effective Behaviour Change Mechanism)

A1. In the business, we have to compete with other companies in searching for suitable customers.

A2. In the business, we need to constantly acquire information about potential business opportunities.

A3. In the business, we need to determine the appropriate terms to offer to win business contracts.

A4. In the business, we need to negotiate contract in order to win them from the competitors.

A5. In the business, we have to closely monitor fulfilment of contracts in order to get repeat business.

A6. In the business, it is important to innovate in order to win repeat contracts.

A7. In the business, it is important to create superior values for the customers to win repeat business.
Ethics Based Feedback System. (Monitoring Aspect)

F1. In this company, managers are concerned about unethical work issues raised by employees.
F2. In this company, employees can openly discuss with managers unethical work issues.
F3. In this company, reports of unethical work issues will be investigated independently.
F4. In this company, employees are willing to report unethical work behaviours.
F5. In this company, managers encourage employees to raise unethical work issues for clarification.
F6. In this company, recurring unethical issues are openly and actively addressed to prevent future occurrence.
F7. In this company, there is a clear mechanism to bring up unethical work related issues.

Ethics based Performance System. (Motivation Aspect)

J11. In this company, employees are willing to break the rules in order to advance their career in the company.
J12. In this company, obeying superior is more important than being honest.
J13. In this company, obeying superior is considered more important than being fair.
J14. In this company, achievement is valued more than commitment and loyalty.
J15. In this company, personal success is more important than helping others.
J16. In this company, employees strive to obtain power and control even if it means compromising ethical values.
J17. In this company, employees are willing to tell a lie if it means advancing their careers in the company.
J18. In this company, In order to control scarce resources, employees are willing to compromise their ethical values.

Corporate Governance (Effective Behaviour Change Mechanism)

C1. In this company, employees I work with act with honesty and integrity.
C2. In this company, employees I work with provide work information that is accurate.
C3. In this company, employees I work with provide work information that is complete.
C4. In this company, employees I work with provide work information that is objective or not influenced by others' interest.
C5. In this company, employees I work with provide work information that is relevant.
C6. In this company, employees I work with provide work information that is timely.

C7. In this company, employees I work with comply with rules and regulations.

C8. In this company, confidential information acquired by employees in the course of their work is used for personal advantage.

C9. In this company, employees proactively promote ethical behaviour with one another.

C10. In this company, employees act responsibly in the use of and control over all assets and resources entrusted to them.

**Ethical Behaviour**

K1. In this company, I know of employees who conceal information from customers that could be damaging to their job performance.

K2. In this company, I know of employees who report performance/financial data to make it seem they are performing better than they really are.

K3. In this company, I know of employees who conceal information from their superior that might be damaging to their job performance.

K4. In this company, I know of employees who withhold negative information about the products or services from customers.

K5. In this company, I know of employees who do not tell the complete truth about the company's products or services to customers.

K6. In this company, I know of employees who do not tell the complete truth to the internal auditor to help make the performance/finances (e.g., revenue, losses, budget, etc.) look good.

K7. In this company, I know of employees who fail to inform customers or clients of important changes to the products or services.

K8. In this company, I know of employees who do not tell the complete truth to the supervisor to help make their performance or finances (e.g., revenue, losses, budget, etc.) look good.

K9. In this company, I know of employees who withhold damaging information from a potential customer about the services or products.

K10. In this company, I know of employees who believe that in order to do their job, it is alright to deceive customers.