



## CAN SMES AFFORD TO BE ETHICAL?

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**T**he value of entrepreneurs and small and medium sized enterprises (SMEs) is widely recognised in terms of the contribution this sector makes to the economy and to job creation. Accordingly, much attention is being focused on how to promote SMEs, as reflected by the government's announcement in Parliament in February 2014 to boost its support for SMEs by R6.5bn over the next three years. Given the growing importance of this sector, it warrants asking how ethics fares for small businesses and whether ethics is less relevant for small-scale operations.

### The costs of being ethical

An argument that is raised against following an ethical approach is that SMEs cannot afford the cost and time that this incurs. However, this view mostly equates ethics solely with compliance. Legal and regulatory compliance can be burdensome for small operations and both the time and cost warrant being minimised. But that should not be confused with running a business ethically, which entails ethical leadership and actions and choices that reflect honesty, responsibility, accountability, fairness and respect. Instead, SMEs should recognise that ethics can serve to differentiate them from their competitors. As such, ethics becomes a strategic advantage that can serve as a catalyst for growth.

Ethics also matters for SMEs in terms of setting a precedent for the future. Ideally, the culture of the start-up operation should provide a sound foundation for the culture of the future corporation it aspires to become. Starting the right way also avoids the 'legacy cost' when earlier unethical practices are held against the company in the future.

A primary fact that is central to the issue of ethics and SMEs is the high failure rate of entrepreneurs who start businesses. According to Bloomberg, 80% of entrepreneurs fail within the first 18 months. The challenge of survival is thus very real. This risk is often increased by how SMEs are treated by their clients. When dealing with large organisations and the public sector, SMEs can be too small to negotiate fair contracts when faced with a 'take-it-or-leave-it' choice. They can also be too small to fight back when treated unfairly. When, for example, the clients refuse to pay the full fee, implying they will follow a legal route to enforce their view, the SME is unlikely to be able to afford the cost of legal help to challenge them – even if they are entirely in the right. Such treatment should be recognised for what it is: the blatant abuse of power. While there is no single way that SMEs can avoid this, they nonetheless need to be wary that they manage the risk in their business carefully. The ideal solution is that large organisations and the public sector accept that they have a moral obligation to treat smaller organisations with fairness and integrity. Crucially, this includes reasonable payment terms.

Limited financial resources often do not allow SMEs to weather the cash flow challenge when payment is delayed. The consequent negative cash flow can force small employers to retrench staff or to incur debt to cover their costs and can even lead to the closure of the business. A recent initiative by the National Small Business Chamber, the Prompt Payment Code, which aims to get government departments and corporates to pay their small suppliers within 30 days, is to be commended. And more can be done by government to drive and monitor prompt payments by all its departments.



### Business survival and rationalisation

The challenge of survival for SMEs brings with it further ethical challenges – specifically whether the pursuit of survival lends itself to cutting corners. For example, can the need to sustain positive cash flows lead to customers being overcharged? Does the pressure to gain access to work lead to false or inflated claims about the company's services, products or expertise? Would the entrepreneur be tempted to offer a bribe (or agree to a request for a bribe) in exchange for a lucrative contract that could support the company's continued existence?

The ethical challenge the entrepreneur faces is between the short-term gain of an unethical approach versus the long-term cost if the misconduct becomes known. This cost can be very damaging to the business, encompassing reputational damage, the erosion of trust with key clients and, in extreme cases, legal action and criminal prosecution. This dilemma is exacerbated by the immediate gain being relatively certain, while the risk of being found out is only a possibility, and by the fact that people often rationalise their ethical choices.

Rationalisation is especially problematic because it rests on the person knowing what is right, but finding a reason or circumstance to justify why unethical action is acceptable.

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The rationalisation can, for example, be based on the claim that it is standard practice or that other people are doing the same things, or on the view that it is not so serious. These arguments are also used to reduce the guilt associated with the misconduct, generally by transferring it elsewhere.

Thus it is likely to be expressed as, ‘I was forced to do so to keep the company going’. But the overarching factor that will dictate how such ethical dilemmas are managed will be the ethics of the leader, be that the entrepreneur or the business owner. Leadership is widely accepted as the most powerful influencer of ethics and this is particularly so in SMEs because, unlike their counterparts in larger organisations, leaders in SMEs are generally not subject to formal governance structures. Therefore, not only does ethics matter a great deal for SMEs, but ethical leadership matters even more.

### ETHICAL CHECKLIST

An ethical checklist is a useful tool to manage ethics relative to specific issues and to ensure that the business looks beyond both the short-term implications of the issue and its own interests in the matter. Pertinent questions would include:

1. Is the proposed action (or choice or decision) legal?
2. Does the action meet the company's ethical standards?
3. Could the action be shared without shame or guilt with others, such as with one's family?
4. How would this action be defined if viewed by outsiders, for example, by the press?
5. Who would be affected by the action and what would the impact be?
6. Does the action set a sound precedent for the future?

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