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EDITORIAL

Dear readers!

The recent issue of the journal is devoted to several governance and regulation issues.

Mária Bordás sheds light on the current tendencies if the international law on warfare can successfully be applied in the practical reality in the progress of counterinsurgency and counterterrorism efforts. There have been two phenomena identified recently in the warfare which are endangering public security and public safety of the democratic states of the world: terrorism and insurgency. Both of them mean a threat and violation to the population and the government authorities.

Daniel Chigudu shows that despite the presence of some regulations public officials manipulate tender procedures for personal gains. There is need for improved political will to enforce the law on errant behavior. The value for money that the procurement system should promote is lost. The article provides recommendations for the government in pursuit of public procurement best practices.

Frank Doussy and Elza Doussy aim firstly to establish whether schools in South Africa comply with the current legislative prescripts and accounting and auditing practices, and secondly to identify possible problem areas in this regard.

Za-Mulamba Paulin Mbecke questions if the management practices and expertise of business could be transferred to the public service and to know what type of management practices and expertise could be transferred and with what adaptations.

Emir Phillips critique's Alexei Marcoux's A Fiduciary Argument Against Stakeholder Theory which set the mark for Shareholder Theory. Stakeholder Theorists sense the denouement of Shareholder Theory, but perhaps this in-depth reassessment of Marcoux's Article may have them reconsidering. Recent corporate scandals reveal only the moral paucity of that company's management and are not conclusive evidence of any odious qualities inherent to either shareholders or Shareholder Theory.

Alexander Maune explore the positioning of the competitive intelligence function within organisations so as to establish the best positioning. To ensure reliability of the literary exploration, only peer-reviewed journal articles were used. The findings of this article will make it possible to generalise about the best position of the competitive intelligence function and to develop some valuable propositions for future studies.

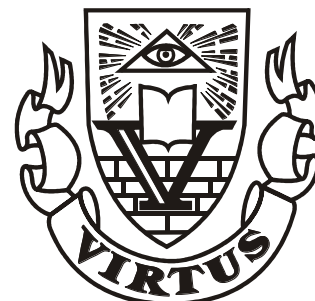
Sivave Mashingaidze provides a framework for understanding and adoption of Business Intelligence by (SMEs) within the Zimbabwean economy. The article explores every facet of Business Intelligence, including internal and external BI as cutting edge strategic asset.

We hope that you will enjoy reading the journal and in the future we will receive new papers, outlining the most important issues in the field of governance and regulation.

JOURNAL OF GOVERNANCE AND REGULATION

VOLUME 3, ISSUE 4, 2014

CONTENTS



Editorial 4

CURRENT ISSUES OF INTERNATIONAL LAW IN REGULATING COUNTER-INSURGENCY AND COUNTER-TERRORISM 7

Mária Bordás

The study sheds light on the current tendencies if the international law on warfare can successfully be applied in the practical reality in the progress of counterinsurgency and counterterrorism efforts. There have been two phenomena identified recently in the warfare which are endangering public security and public safety of the democratic states of the world: terrorism and insurgency. Both of them mean a threat and violation to the population and the government authorities. It has been queried in the military literature whether these new forms of warfare should be handled by military engagements or law enforcement. This is, nevertheless, not just a dilemma of the strategy how to combat against it, but should be, at the same time, in accordance with the international legal regulations, too.

PUBLIC PROCUREMENT IN ZIMBABWE: ISSUES AND CHALLENGES 21

Daniel Chigudu

With negative coverage largely by the media on state procurement, this article aims at exploring challenges and issues that militate against public procurement in Zimbabwe. The exploration is done through content analysis of statutes and procurement practices that currently obtain in the country. The study shows that despite the presence of some regulations public officials manipulate tender procedures for personal gains. There is need for improved political will to enforce the law on errant behavior. The value for money that the procurement system should promote is lost. There is no mechanism for feedback to inform management and policy makers. The article provides recommendations for the government in pursuit of public procurement best practices.

FINANCIAL STATEMENTS AND THE DISCHARGING OF FINANCIAL ACCOUNTABILITY OF ORDINARY PUBLIC SCHOOLS IN SOUTH AFRICA 27

Frank Doussy, Elza Doussy

The Schools Act, 84 of 1996 (section 42(b)), requires that all public schools in South Africa, “as soon as practical, but not later than three months after the end of each financial year, draw up annual financial statements”. These schools must further submit audited financial statements to the Department of Education within six months after the school’s year end (section 43) and according to section 43(6), “at the request of an interested person, the governing body must make the records referred to in section 42, and the audited or examined financial statements referred to in this section, available for inspection”. The study aims firstly to establish whether schools in South Africa comply with the current legislative prescripts and accounting and auditing practices, and secondly to identify possible problem areas in this regard.

OPERATIONS AND QUALITY MANAGEMENT FOR PUBLIC SERVICE DELIVERY IMPROVEMENT 36

Za-Mulamba Paulin Mbecke

The initial questions of this research were to establish if the management practices and expertise of business could be transferred to the public service and to know what type of management practices and expertise could be transferred and with what adaptations.

A BAYOU PRIVATEER CRITIQUE'S MARCOUX'S FIDUCIARY ARGUMENT AGAINST STAKEHOLDER THEORY 46

Emir Phillips

This Article critique's Alexei Marcoux's A Fiduciary Argument Against Stakeholder Theory which set the mark for Shareholder Theory. Stakeholder Theorists sense the denouement of Shareholder Theory, but perhaps this in-depth reassessment of Marcoux's Article may have them reconsidering. Recent corporate scandals reveal only the moral paucity of that company's management and are not conclusive evidence of any odious qualities inherent to either shareholders or Shareholder Theory.

COMPETITIVE INTELLIGENCE: AN EXPLORATORY LITERATURE REVIEW OF ITS POSITIONING 61

Alexander Maune

This article is a qualitative-exploratory literature review. The primary concern of the author is to explore the positioning of the competitive intelligence function within organisations so as to establish the best positioning. To ensure reliability of the literary exploration, only peer-reviewed journal articles were used. The findings of this article will make it possible to generalise about the best position of the competitive intelligence function and to develop some valuable propositions for future studies. The findings show that there is no single criterion on which to base the positioning of the competitive intelligence function within organisations. This article will assist business managers to understand and improve their positioning of the competitive intelligence function. This article has therefore academic value.

DESCRIPTIVE BUSINESS INTELLIGENCE ANALYSIS: CUTTING EDGE STRATEGIC ASSET FOR SMES, IS IT REALLY WORTH IT? 70

Sivave Mashingaidze

The purpose of this article is to provide a framework for understanding and adoption of Business Intelligence by (SMEs) within the Zimbabwean economy. The article explores every facet of Business Intelligence, including internal and external BI as cutting edge strategic asset. A descriptive research methodology has been adopted. The article revealed some BI critical success factors for better BI implementation. Findings revealed that organizations which have the greatest success with BI travel an evolutionary path, starting with basic data and analytical tools and transitioning to increasingly more sophisticated capabilities until BI becomes an intrinsic part of their business culture and ROI is realized.

SUBSCRIPTION DETAILS 84

CURRENT ISSUES OF INTERNATIONAL LAW IN REGULATING COUNTER-INSURGENCY AND COUNTER-TERRORISM

Mária Bordás*

Abstract

The study sheds light on the current tendencies if the international law on warfare can successfully be applied in the practical reality in the progress of counterinsurgency and counterterrorism efforts. There have been two phenomena identified recently in the warfare which are endangering public security and public safety of the democratic states of the world: terrorism and insurgency. Both of them mean a threat and violation to the population and the government authorities. It has been queried in the military literature whether these new forms of warfare should be handled by military engagements or law enforcement. This is, nevertheless, not just a dilemma of the strategy how to combat against it, but should be, at the same time, in accordance with the international legal regulations, too.

Keywords: International Law, Counter-Insurgency Regulation, Counter-Terrorism Regulation

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“Inter Arma Enim Silent Leges” (In times of war the law falls silent) / Marcus Tullius Cicero/

Introduction

This study tries to shed light on the current tendencies if the international law on warfare can successfully be applied in the practical reality in the progress of counterinsurgency and counterterrorism efforts. There have been two phenomena identified recently in the warfare which are endangering public security and public safety of the democratic states of the world: terrorism and insurgency. Both of them mean a threat and violation to the population and the government authorities. It has been queried in the military literature whether these new forms of warfare should be handled by military engagements or law enforcement. This is, nevertheless, not just a dilemma of the strategy how to combat against it, but should be, at the same time, in accordance with the international legal regulations, too. The international law of war developed by the end of the 2nd World War was basically modeled to the traditional - symmetric - warfare. After the 2nd World War the main form of warfare has been much rather asymmetric, than symmetric. We can state that both insurgency and terrorism represent an asymmetric warfare. Traditional warfare became rather exceptional[15], but insurgency with the characteristics of terrorism became the rule during the last decades.

The starting point of this study is that similarity between insurgency and terrorism seems to be more important than to make by all means sharp division between them. This is because the international law from many aspects does not differentiate the groups with armed forces if they are insurgent or terrorist, or has other terminologies than the military science. When this study is going to outline how the international law based on the principles of traditional warfare can be applied to insurgent or terrorist groups, special emphasis will be given, if the relevant laws have failures in regulating these new forms of warfare, and if so, what changes should be proposed for the recent regulations of the international law.

1. Attempts for Defining Insurgency and Terrorism

Several definitions of insurgency and terrorism have been identified in the military literature, which at the same time try to make distinction between them. Phrases, like insurgency, irregular warfare, unconventional warfare, revolutionary warfare, guerilla warfare, terrorism are often used in the military literature as synonymous terminologies.[8] This is because all of these forms of armed conflict mean an asymmetric warfare. Further similarities, such as committing terrorist attacks, pursuing radical aims, intimidating civilians, etc., have been seen in these forms of warfare. It should be noted that *terminology of insurgency* can be used to the armed troops in revolution, freedom fight, guerilla war and

civil war, because the latter ones all have the political and military characteristics of insurgency.

Symmetric warfare has been identified as two opposing adversaries dispose of armed force that are similar in all aspects such as force structure, doctrine, asset, and have comparable tactical, operational and strategic objectives. Traditional warfare took place in most cases between state regular armies until the middle of the 20th century. Insurgencies – typified as *asymmetric warfare* – could be seen even before the 2nd world war[2], but were not widespread. Asymmetric warfare – as opposed to symmetric warfare - means that the opposing party is unable or unwilling to wage the war with comparable force, and has different political and military objectives than its adversary. These new forms of the asymmetric warfare are not just emerging political or military issues in our days, but a confused legal problem, too. In other words, terrorism and insurgency is not just an academic legal issue, and it is not the same how the laws define them. This is because sanctions, criminal consequences, investigating authorities, jurisdiction, military response, intelligence and law enforcement, etc. as the legal issues of terrorism and insurgency should sufficiently be regulated by the international and domestic laws.

Insurgency has been defined with the following characteristics[11]:

- *Organized movement* of a group, which, at the same time, leads to a protracted violent conflict.
- The involved groups' aim is to *overthrow the constituted government, or fundamentally change the political and social order* in a state or a region, or *weaken the control and legitimacy* of the established government.
- The means of an insurgent group to reach their aims are *subversion, armed conflict, sustained violence, social disruption and political actions*.
- Their aim has been rooted in the claim for *autonomy or independency* for an ethnic minority, a *more democratic government, or political and economic rights* to a social class.

All the definitions of the *terrorism* emphasize that terrorists use *violence and threat* against the population, property, places of public use, public transportation system, infrastructural and other facilities in order to reach a *general fear* in the society with *political, ideological or religious* aims.[13] Terrorist attacks – as opposed to insurgency – are normally *unpredictable and random* in order to trigger psychological effects, i.e. *intimidation and government overreaction*. Terrorist groups are *clandestine* agents increasingly on *transnational level*. It is an essential question as to whether on the basis of definitions of insurgency and terrorism we can make *clear difference* between them. Both of the insurgents and terrorists are based on violence in actions, have political aims, and insurgent groups use not just mean guerilla warfare, but often commit terrorist attacks, too, or similarly to the terrorist

groups, are financed from organized crimes. Terrorist groups, on the other hand, are often also well-organized, and tend to escalate the violent conflict.

Some differences between them, however, are *typical*: insurgent groups, for example, try to control one of the territories of the state, while terrorists normally not, insurgents occasionally respect the law of war, but the terrorists never, insurgents try to have the support of the population, while it is not important for terrorists, insurgents do not necessarily attack civilians, but it is the rule for terrorists. We can mention as *examples of overlapping* in some groups that have characteristics of an insurgent group, despite they are considered terrorists. *Al Qaeda* has a worldwide network, and regularly infiltrates insurgent groups in other countries, such as Iraq, Afghanistan and Syria. The *Hamas* forms the part of the Palestine Authority and the *Hezbollah* has 11 seats in the Lebanese government, so they are in fact state authorities implementing social welfare tasks, too.[4] *Hezbollah* is evidently a terrorist group, and the military faction of the *Hamas* has also been pronounced so by the European Union some months ago.

The *Chechen in Russia* have all the characteristics of an insurgent group, e.g. they form an organized group of an ethnic minority in a given territory of the state, claim autonomy or an independent state for them, and use political means, military force against the government, however they have been on the blacklist of the terrorist groups, due to the terrorist attacks they implement. Insurgent groups in the war in *Bosnia* and *Kosovo* during the 1990-s with the same characteristics were considered as insurgents, but not terrorists. Both the *ETA* and the *IRA* have a double face in their warfare: their strategy is similar to the terrorists, e.g. they attack civilians and do not want to acquire territory, but they are typified at the same time by guerilla warfare, e.g. exploited bridges or attacked police stations.

Overlapping is even more complicated in the *Palestine Liberation Front*: its groups of a few members crossed the border of Israel and exploited objects and crowded places, took hostages, attacked villages and killed civilians. These Palestine terrorist groups controlled territories both in Lebanon and Jordan where recruited members and had terrorist training camps, too, but implemented armed attacks in the area of Israel. The insurgent groups in *Afghanistan* and *Iraq* perpetrated terrorist attacks against the civilians in the way of suicide bombings, exploiting international organizations, embassies, schools, markets, etc., but as well as guerilla attacks by using traditional warfare against military bases of the Afghan army or the NATO. It should be clear on the basis of these examples, that *insurgent groups use terrorist means, too*, if they see it more efficient than the guerilla warfare, or, in many cases they did not have any other choice than to do so, either, because of the special fields, e.g. high hills, or jungles, where

they fight. It can happen sometimes that not just the insurgents, but also the *terrorists are supported by the civilians*, as it was the case in Iraq, where the Sunni tribes had cooperated with Al Qaeda until they became fed up with the frequent terrorist attacks. In Afghanistan, where the Al Qaeda has been interwoven with the Taliban, and commits terrorist attacks together with them, the Al Qaeda enjoys the support of the local tribes. It would be difficult, too, to find a terrorist group that does not pursue *concrete political aim*: the Al Qaeda aims to establish a world caliphate based on the fundamentalist Islam culture and destroy the West, the Hezbollah supports insurgent groups in other countries, such as Iraq and Syria with political goals, and the Hamas aims to eliminate the Israeli state. Even those terrorist groups, such as the Muslim Brotherhood, the AQIM, Al Shabaab, etc., which ideology represents only religious features on the surface, i.e. the fundamental Islam, are deeply rooted in politics, when aim to fight against the secularization, or try to hinder a more democratic process in Muslim countries.

Local militias in African countries, e.g. Mai-Mai in Congo, LRA in Uganda, NPF in Liberia, etc., often *do not follow any political aim*, even if they are supported by the Al Qaeda, or other terrorist groups, they just use the advantages of a weak government that cannot efficiently control some areas of the state and try to maintain themselves from certain crimes and violent actions against the civil population.[5]

Militias otherwise have all the characteristic of insurgents, but cannot be considered so, much rather simple *criminals*. In order to make *distinction* between insurgency and terrorism, the most important point of view is as to whether they commit common crimes or use lawful armed force. When doing so, we have to face up to further issues: if the insurgents perpetrate violate actions, they should be considered terrorists? When insurgents seriously violate the international law, for example attack civilians, civil objects, kill the prisoners, etc., they evidently cannot be identified as lawful combatants. The problem with it is that insurgents often go beyond this, and commit organized crimes, as well, e.g. drug trafficking, smuggling of weapons, taking of hostages, money laundry, etc., in order to finance their activities. This is because insurgents in most cases try to counterbalance their asymmetric position against the state regular army which necessarily leads to the violation of the law on warfare and the criminal law.

After having analyzed the differences, it should be clear that we cannot identify any insurgent or terrorist group that would have only terrorist or insurgent characteristics. As we could see from the aforementioned examples, *there are no clear insurgent or terrorist groups in the practical reality*, but non-state armed troops having more or less features of insurgency, terrorism or organized crimes.

2. Challenges of the Legal Regulations in Counterinsurgency and Counterterrorism

There are two legal status in the international law with regard to armed troops: the *law of war* differentiates if they meet the requirements of a regular army (having uniforms, or distinctive sign, carrying arms openly, being under responsible command and respecting the law of war) and the *law of humanitarian treatment* makes difference on the basis of having a war character, or not. Consequently, an insurgent group will be considered to be under the force of the law of war, and the law of humanitarian treatment, if they meet the aforementioned requirements. If not, they – similarly to the terrorists – will be treated as *criminals*. When the insurgents are under the force of the international law on warfare, they have to respect the law of war and the law of humanitarian treatment, and in return, they will be treated by the state regular army as combatants of warfare.

The armed conflict between the insurgents and the government army will be subject to a *military engagement* on the basis of the rules of war. If insurgents are considered as criminals – when they commit terrorist and organized crimes, or crimes “just” against the public safety, public order or the state power¹ – they will be put under the force of *law enforcement*, i.e. come up for trial based on the rules of the criminal procedure. When people offend or would like to remove the existing government other than by democratic elections, *it is always unlawful according to domestic laws*. The peaceful demonstration permitted by the public authorities is the only exception. In other cases, when citizens are unsatisfied with the government, and express it in *violent actions*, such as riot, conspiracy (Bolshevik Party in Russia) revolution (fundamentalist Islamists in Iran) freedom fight (Che Guevara in South America) guerilla war (Taliban in Afghanistan) civil war (Syria) military putsch (Chile) domestic laws normally regulate it as *crimes against the state power*.

On the other hand, however, the *international law entitles the state to use military force in self-defense*, when an armed attack has occurred in the boundaries of the state, even if the insurgent group is not under the law of war. (Article 51 of the UN Charter) The only limitation for the state in crushing the insurgency is to respect human rights and international criminal law. If the insurgency has been crushed, the state uses *criminal enforcement*: arrest, trial and punishment. It is possible that the government gives *amnesty* to the insurgents after the

¹ Insurgents – according to the domestic laws – are always in an illegal position, unless they do not commit violate actions, e.g. in the case of a peaceful demonstration permitted by the state authorities, because every violent action against the state power, are regulated by the laws as crimes in most countries.

insurgency has been crushed, which reflects to the political compromise has been made between the insurgents and the government. When the insurgency wins, and the insurgents can establish a new state on the territory where the ethnic minority lives, or if they can overthrow the government, the other states, according to the international customary law, will *approve the new state or government*, provided it is operating efficiently. A new state or a new government are just rarely come into existence in a lawful way - Hungary and Germany can be mentioned as examples in 1990 - the majority has been as a result of revolution, insurgency, freedom fight, or military putsch. *Legitimacy* evidently lacks in the latter cases. International customary law expects, for this reason, the new state or the government to consolidate its legitimacy with election or referendum.

Distinction between insurgency and terrorism in the international law *is not accordance* with the new challenges of asymmetric warfare. When governments have to face up to the problem of insurgency or terrorism, they cannot achieve any decision on the basis of such legal issues, whether to use military engagement or law enforcement, because in most cases it would go *against the rationality*. As mentioned earlier, there is no clear difference either in the theory or in the practice between insurgency and terrorism.

Military engagement is often *necessary* against terrorist groups, e.g. in Afghanistan or Iraq, where law enforcement would obviously be inefficient. Or, when Bin Laden, who was a terrorist, not an insurgent, had to be liquidated, the special forces of the US Army implemented a military operation. As another example, the Israeli Army in more cases attacked Gaza and South Lebanon and used its military armed forces, as a reaction to the terrorist attacks from these areas. The government can successfully use the armed forces of the police when a riot has broken out, for example, but against most terrorist organizations it'd be a failure. It does not seem to be reasonable, either, from the side of the government army to respect the rules of war when insurgents or local militant gangs perpetrate terrorist crimes, even if they should be considered as a regular army by the laws. The problem, from legal point of view, is even more complicated when the insurgents or terrorists have been *captured*: they should be treated as criminals, and if so, which court will have the competence to proceed in the criminal case? Examples of the prisoners in Guantanamo Bay and Abu Graib led to a widespread debate in the US, if the human rights of the captured terrorists, such as the right to life, human dignity, and fair jurisdiction, should be respected, or not. Preconception can be made on the basis of this exposition that regulations of counterinsurgency and counterterrorism are fairly *vague* in the international law, and should be adjusted to the *new challenges of asymmetric warfare*.

3. Characteristics of the International Law of War

The first attempt to codify the law of war happened in 1863, in the midst of the American Civil War. President Lincoln asked Francis Lieber, a jurist and political philosopher, to draft a code of warfare in order to regulate the armed conflict. The so called "*Lieber Code*" – served as a base for the Geneva Conventions - regulates instructions for the Government Armies of the US in the field. Its 157 articles were concerned with martial law, military jurisdiction and the treatment of spies, deserters and prisoners of war.[12] The *recent sources of the international law regulating warfare* are as follows:

- Geneva Conventions and its protocols
- Hague Conventions and its protocols
- United Nations Charter
- International Criminal Law
- Treaties on Human Rights
- Rules of Engagement

Recently, the law of war has been regulated by the international law, not by the domestic laws. International law has *two main characteristics*, which determine the applicability of the law of war, too. One is that the provisions of the international law shall obligate a state, only if it has ratified an international contract, but only in the framework of this contract. For example, if a state has not signed the Geneva Conventions, it is problematic, how to have it kept the rules of the prisoners of war.

Certain organizations of the European Union have supremacy to pass legal norms, and apply them by the courts, even if it is against the member states' domestic laws. The EU law is called, for this reason, as "*sui generis*" law.[9] International organizations, such as the United Nations itself, *do not have the right to regulate international affairs*, because only the international treaties, charters, conventions, etc. can do so. So, only the provisions of the UN Charter shall be applied and only to its signatory nations. Or, the UN Human Right Committee, for example, cannot make any obligatory decision in the legal cases of human rights to the signatory nations, just give recommendations to them. The international law – as opposed to domestic laws – has been based on mainly the *cooperation* among the nations rather than that of the *law enforcement*.

The latter one is, however, the essential part of the domestic laws, because the state can enforce its will only if uses its political power thorough the legislation, the public administration, and jurisdiction. The legal norms passed by the parliament or the administrative authorities can be implemented only by the use of law enforcement, such as police, prosecutions, courts, prisons, etc. Sanction has normally been an essential part of the legal norms in the domestic laws: when the provision of the law is not implemented voluntarily, the sanction should be applied by the state authorities. Law enforcement has

been the rule in domestic laws, and alternative means, such as the use of mediators in the trials, or the declarations in the legal norms are rather exceptional.

The prevailing legal means in the international law are several forms of *cooperation*, e.g. establishing ad hoc committees, organizing conferences, writing reports, recommendations, diplomatic negotiations, mediating peace, etc. *reprisal* and *retortion* can legally be used against a state, if it violated the international law, so that lawful actions can be enforced. The most traditional sanction, *to start a war* against a state violates the recent international law, so it cannot be widely applied anymore, just in exceptional cases regulated by the international law. There are *two exceptions*, when despite the lack of law enforcement character the provisions of the *international law can be enforced*. The Security Council of the United Nations is empowered by the Article 42 of the UN Charter to authorize member nations *to use military force* to deal with any situation that the Council determines to be threat to international peace, a breach of the peace or an act of aggression. This provision can be used only when other means, such as diplomatic measures or economic sanctions have been or would be ineffective to deal with the threat. The other exception is the *International Criminal Court* that will open a criminal procedure against the criminals who have perpetrated international crimes, even if the state, whose citizens are the criminals, is unwilling to, or cannot do so. The military leaders of the former Yugoslavia were punished in this way.

International law is generally considered as “*soft law*”, which is its other characteristic. It means that legal norms of the international law are so generally formulated that in the concrete cases it can be interpreted in several ways. The interpretation of the legal provisions depends to a great extent on the political power of the states that will apply them in the practical reality. The US and Great Britain interpreted the provisions of the Article 51 of the UN Charter in the way, that they had the right in self-defense to attack Iraq in 2006, however one of the essential conditions, i.e. the armed attack by Iraq against these countries missed. There are “*ius cogens*”, not just “soft” legal norms, too, in the international law, such as the prohibition of the use of force, non-intervention, or human rights, for example, which means that these legal institutions have been interpreted in the legal practice by the international organizations as a case law and will be implemented, if possible, in a strict way.

The *international customary law* means those rules, that have been widely and for a long term applied in the practice, based on international treaties, conventions, agreements, charters, declarations, or covenants, and have a uniform interpretation. Rules of engagement issued by the commandant, for example, can be mentioned as customary law, because its provisions are not legal norms, but should

be based on the international law on warfare. Acknowledgement of a new state by the other ones can be mentioned as an example to the customary law. Human rights are formulated as *legal principles* in the international agreements.[14] This is a reason, why the interpretation of human rights so important, either in the way of case law, as it has been a tradition in the common law, or in the practice of jurisdiction similarly to the European continental laws.

4. The Law of Humanitarian Treatment and Human Rights

The Geneva Convention is called as international law for the *humanitarian treatment of war*, but the Hague Convention is the *law of the war*. At the moment, with one exception, every country of the world has already ratified both the Geneva and Hague Conventions, but not all of their protocols. The only exception is West Sahara, which has been occupied by Morocco, so it does not have independent state-system to achieve its own decision.

The Geneva Convention consists of 3 conventions and 3 protocols.[7] They regulate the treatment of the *wounded, sick and shipwrecked*, the *prisoners of war*, the *civilians* and the *victims*. The most important rules for the treatments:

- Prisoners of war (the captured combatants) cannot be attacked any more, but should be spared, and have the right to human treatment, such as health care, clothes, food, personal property, decorations, badges of rank, payment for their work, correspond with their relations, etc.
- Wounded, and sick have the right to medical treatment, evacuation, but the dead have the right to medical examination about the death, identification, collection of their bodies and remains, burial according to the rites of their religion.
- Civilians who do not take active part in the armed conflict and the combatants who have ceased to be active, have the right not to be attacked, compensation for their injuries, death damages in their property, and for being refugees.
- Violence to life, persons and human dignity, such as murder, mutilation, cruel treatment, torture, degrading treatment with the prisoners of war, the sick, the wounded and the civilians, also taking of hostages are prohibited.
- Carrying out executions is also prohibited, unless previous judgment pronounced by a regularly constituted court, with all the judicial guarantees. Prohibition of execution does not mean the pure killing, rather the right to a fair jurisdiction.

The provisions of the Geneva Convention shall be applied in the following cases:

- *Declared war* between the signatory nations.

- If the opposing nation is not signatory, when it accepts the Convention.
- If *the armed conflict happened in the boundaries of the country* between the government army and the insurgent group, or two insurgent groups, provided it has a war character.

Enforcement of the provisions in the Geneva Conventions is less problematic, when there are two or more states in the armed conflict, however enforcement cannot happen in a direct way even in these cases. Using a *protecting power (mediator)* selected from those states that did not take part in the conflict, but agreed to look after the interest of a state that is a party to the conflict has been the most common way to manage the conflict. The “mediator” state has the competence to establish communication between the parties of the conflict, monitor the implementation of the Conventions, visit the zone of armed conflict and advocate the prisoners of war. Geneva Conventions will be applied in the case of insurgency, too, if it has a *war character*, which is a widely debated issue. It has been queried for example, how to know if an insurgency has a war character, or not, when this terminology has neither been defined, nor interpreted. Nevertheless, the *definition of insurgency* has not been identified by any international legal regulation, either. As mentioned earlier, there may be armed conflicts with war character between the government army and the local militias, when the militias cannot be considered by the military practice as insurgent groups, but local criminal gangs. Can we draw the conclusion that the government army and the local militia do not have to respect the provisions of the Geneva Convention in such cases? On the basis of the relevant legal regulations, there is no answer to this question. It is another matter, if in the lack of clear regulations sufficient solutions have already developed in the practical reality.

Further questions will be raised: if the insurgents perpetrated terrorist and organized crimes can be treated as prisoners of war, after they have been captured, in the way it is identified in the Geneva Convention, or, they should be sent to trial as soon as possible? Or: who is entitled in such cases to investigate if they are suspicious with committing crimes, which should base a criminal procedure against them? These are, however, not just theoretical questions. After the prisoners had been kept in Guantanamo for five years, it turned out that only a few of them were terrorists. Terrorist in Afghanistan, Pakistan and Yemen, for example, have been liquidated in a targeted killing, without any judgment made by a court. The provisions of the Geneva Conventions do not determine the legal status of the opposing parties in the internal armed conflict. The government is entitled to treat captured insurgents as criminals by its domestic law, even if they are under the force of the Geneva Conventions and ought to

treat as prisoners of war. It should be noted that there is no agreement among the legal scholars as to whether or not there exists international law of armed conflict that shall be applied in the internal armed conflict.

This challenge has been justified by the legal disputes in the US, when the Supreme Court in the *Hamdan case* (Hamdan had been Bin Laden’s driver and bodyguard who was captured in Afghanistan and held in Guantanamo Bay)² declared that the armed conflict caused by the Al Qaeda terrorist attacks does not have an international character, but happened on the territory of a party of the Geneva Conventions. For this reason, not all the provisions of the Geneva Conventions shall be applied, but only the Article 3, that determines *the rights* of the unlawful combatants *to a fair trial*. *Human rights* should also be examined from the point of view of its relevance in the counterinsurgency and terrorism. Human rights were first regulated by the Universal Declaration of Human Rights developed by the General Assembly of the UN in 1948. The most important agreement, the International Covenant on Civil and Political Rights came into force in 1976. Customary international law of human rights has also been created as a result of a consistent practice.

Human rights related to terrorism and insurgency are listed in the international law, on one hand as *minimum standards during the investigation*, arrest, detention, trial and punishment, but also as *the right to self-determination*, which is the right of people to independent, democratic institutions free from outside interference, on the other hand. This is a question how the human rights shall be applied in the affairs of wars, insurgencies, terrorism, and other armed conflict?

As we could see in the analyses above, the Geneva Conventions shall not be applied in every internal armed conflict, because of the vague legal regulations. Human rights, for this reason, have a *subsidiary role* in the legal practice. When the Geneva Conventions cannot be applied, human rights having an *“ius cogens” character* in the international laws cannot be violated by the state, non-state groups or individuals, no matter what kind of armed conflict, and on which place occurs. However, the US legal practice did not accept that every provision of the Geneva Conventions shall be applied to the prisons in Guantanamo Bay the public authorities of the US struggled for 5 years to determine their human rights, especially the interpretation of the torture. Prisoners were finally taken to trial, although not in a reasonable length of detention. Opportunities *to enforce human rights* do not show a uniform picture in the international law. Neither the *UN Human Rights Council*, nor the *UN Human Right Committee*

² Emily Bazelon Invisible Men: Did Lindsey Graham and Jon Kyl mislead the Supreme Court?,— *State Magazine* downloaded from http://www.slate.com/articles/news_and_politics/jurisprudence/2006/03/invisible_men.html website

has the right to make decision in the concrete cases, but investigate individual complaints, review fulfillment of human rights, analyze reports, give comments and opinion, mediate peace, etc. Only the *Security Council* has the right to take actions, such as economic sanctions, peace enforcement, and creation of International Tribunals for prosecution and punishment of human rights violators, against the states violated human rights in relations with the threat to the peace and breach of the peace, or acts of aggression. In spite of the fact, that neither the UN Human Rights Council nor the UN Human Right Committee has the right to make decision in the legal cases of human rights, they successfully developed a *case law system*, which serves as a base for the interpretation of human rights in the concrete cases.

The European Union has established the *European Court of Human Rights* that is entitled to make judgment obligatory for the member states in human rights cases. The ECHR applied human rights in the legal cases of armed conflict in more times. Right to life was interpreted, for example, when civilians were killed in the armed conflicts. The ECHR developed a strict interpretation in this matter: when combatants are among civilians and begin to attack the enemy, an offensive operation can be implemented, only if it is necessary to protect civilians, or, if civilians who are taking part in the attack do not react to the warning.

The *importance of human rights* in the armed conflict has been growing, because the traditional law of humanitarian treatment cannot be applied in asymmetric warfare, like insurgency and terrorism. Human rights can serve as a limitation both for the parties involved in the armed conflicts, in the lack of sufficient legal regulations on warfare.

5. The Law of War I. (Ius in Bello)

The first Hague Convention was ratified in 1899, the second in 1907, but the conference where the third convention would have been negotiated, was cancelled due to the start of the 1st World War. The *Hague Conventions* have three main parts:

- *Law of War* (ius in bellum) regulates the means and methods in war, such as injuring the enemy, attack, defense, military movement, treatment of spies, use of the white flag, capitulation, armistice, occupied territories and protected objects and zones.
- *International war crimes*: genocide, crimes against humanity and aggression.
- Regulation of *prohibited/restricted weapons*.

The law of war shall be applied to the combatants of armies, militias and other voluntary groups, if they wear uniform or distinctive sign (badge, armband) carry arms openly, operate under responsible command and respect the law of war and customs. Interpretation of this legal provision is fairly ambiguous, because besides the government armies it

has been extended to other military groups, as well. It is easy to identify if the combatants of a military group meet the requirements of a *regular army*. If the military groups *do not respect* the law of the war, the government army does not have to do so, either. In other words, if an insurgent group implements terrorist attacks against the government army, as it occurs in Afghanistan by the Taliban, the government army will be entitled to attack the military group (insurgent group or militia) with other means, too, than regulated by the law of war.

We could hardly mention such an example from the cases of last decades, when in the asymmetric warfare the insurgent group would have respected the law of war. Consequently, these regular armies normally implement other military engagements, than based on the traditional warfare regulated by the Hague Conventions. *Targeted killing*, such as liquidation, combat drones, air bombing, or *special operation* and *intelligence* as examples can be mentioned to this new way of military engagement.[10]

It is important to query, too, that if Hague Conventions are not applied anymore in most cases, is there any law that would regulate these military engagements? If not, we can draw the conclusion that asymmetric warfare is *unregulated* by the international laws, and the parties involved in the armed conflict are not limited by any rule, except the international crimes, and the human rights.

Enforcement of the law of war is also problematic. The *International Court of Justice*, or the *International Law of Arbitrary* will proceed, but only if the parties in the conflict will entitle them to do so. These courts, however, cannot make a judgment that can be enforced to the states. This is why only 200 cases were taken to these courts during the last 90 years. If these courts do not proceed in the case, consultation, diplomatic negotiation will be applied, ad hoc committee will be set up, or conference will be organized to give recommendation to the parties in the conflict. The state that violated the law of war should pay compensation to the victims and the state that suffered unlawful actions.

International criminal law called in the legal terminology as "*delicta iuris gentium*" was born in 1945, after the 2nd World War, when the Nazi war criminals had to be punished. Earlier it belonged to the issues of state sovereignty to regulate an act as a crime.

The following crimes have been regulated by the international law as crimes: *genocide*, *crimes against the humanity*, *war crimes* and *crimes related to aggression*. Crime against humanity can be murder, torture, slavery, deportation, imprisonment, sexual harassment, chasing of groups, etc. war crimes are regulated by the Geneva Convention, such as attacking civilians, killing wounded, or combatants when they surrendered, humiliating war of prisoners,

taking of hostages, execution without judicial guarantees, etc .

The relevance of it is that these acts shall be considered as crimes, even if the domestic laws of the states do not regulate them so, and people regardless of being combatant of a regular army, insurgent, terrorist or civilian will be taken to trial before the International Criminal Court. The *International Criminal Court* was established in 2002 in Hague, and at the moment 122 states are its members. The International Criminal Court *has the competency to open a criminal procedure against a person committed international crimes*, if the person is the citizen of a signatory state, or, the crime was committed in the area of a signatory state. In other cases, especially if the host state is unwilling or not capable to investigate the case, the Security Council has the right to decide the case will be sent before the International Criminal Court. At the moment there are 12 persons (from Uganda, Congo, Republic of South Africa, Darfur) who are under criminal procedure initiated by the International Criminal Court. The United Nations has the right to establish *ad hoc international criminal courts*, too.

Such courts proceeded first in the criminal cases of Nazis in 1945 in Nurnberg, and later against the criminals of the former Yugoslavia, Rwanda, Sierra Leone, Cambodia and Lebanon.

6. The Law of War II. (Ius ad Bellum)

The right of the states to *start a war* against other states was not prohibited by any law until the 20th century. The provisions of the Hague Convention passed by the Conference in 1907 required only the declaration of war before the state attacked the other one. The new legal regulation which shall apply to the “*ius ad bellum*” was passed after the 2nd World War by the *United Nations*.

“*Ius ad bellum*” is the right of the states to use force against other states regulated by the UN Charter, but can be applied only in exceptional cases. The Article 2 (4) of the UN Charter *prohibits the member states to threat or use of force* against territorial integrity or political independence of any state, or in any other manner inconsistent with the purposes of the United Nations. The Article 2 (1) of the UN Charter declares the *sovereign equality* of the member states, which should be interpreted as the *prohibition of state intervention* in another context. The Article 2 (7) of the UN Charter explicitly prohibits the United Nations to intervene in matters which are essentially within the domestic jurisdiction. In other words, prohibition of the use of force and prohibition of state intervention is the rule in the UN Charter, which gives priority to the *peaceful settlement of disputes* in the maintenance of international peace and security, such as negotiation, mediation, conciliation, arbitration, judicial settlements, etc. in the Article 2 (3) of the UN Charter. These principles

of the UN Charter are interpreted in the declarations of the General Assembly and the resolutions of the Security Council.

Regarding the insurgency and terrorism, we need to know which cases shall be under the provisions of the *UN Charter*, and which ones will be subject to *domestic criminal law enforcement*. It is *the right of the Security Council* to determine the existence of any threat to peace, breach of the peace, or act of aggression, then to make recommendations, or decide what measures shall be taken (Article 38 of the UN Charter) The Security Council, as a first step, tries to apply *measures*, such as interruption of economic relations, means of communications, such as rail, sea, air, postal, telegraphic, radio, etc., and diplomatic relations. (Article 41 of the UN Charter) When these measures seem to be inadequate, the use of *demonstrations, blockade and other operations* by air, sea and land forces is allowed in the case of threat to peace, breach of the peace and aggression. (Article 42 of the UN Charter)

According to the Article 42 of the UN Charter, the Security Council has the right to use *military force*, or may authorize a member nation to do so, if the Security Council determines to be a threat to, or a break of the international peace, and aggression, provided the aforementioned conditions are met, and the diplomatic measures and economic sanctions seem to be inefficient to manage the situation. More resolutions of the Security Council during the 1970-es interpreted the *aggression*: using weapons and armed force, declaring war, invading, occupying or bombing the territory of the state, blockade, sending armed gangs, irregular army or mercenaries, etc. shall be considered as aggression.

It is important that *only the Security Council has the right to use*, or authorize for the use of *military force*, because the definition of the aggression given by the UN Charter is only in the form of exemplary list of acts, which can be interpreted by the states involved in the conflict in more ways. The practical reality shows, that the states do not often admit that they have violated any international law, but often accuse the other one to provoke the conflict, and refer to it as a base to their reaction, or consider themselves in the conflict as the victims of the aggression, but not the aggressor. There happened cases when the state thought political benefit from attacking another state more important than to respect the international laws. The most pregnant example to this is the several conflicts between Israel and its neighboring countries.

The resolution passed by the Security Council on the use of military force is based on unanimous voting of the members of the Security Council, which represents a strong support of the member nations on one hand, but can be a hinder in achieving the decision, if the political standpoints of one or more member states are different. The Security Council consists of the strongest states of the United Nations, for this reason its resolutions are *not independent*

from the actual political interests of its members. Furthermore, it has the exclusive right to interpret the generally formulated “threat to peace and breach of peace” or “international peace and security” legal terminologies. It has been *tangible* on the basis of the resolutions of the Security Council *how political views of its members influence the decisions*.

The Article 51 of the UN Charter regulates the right to *self-defense*. When armed attack has occurred, the nation may use military force in individual self-defense, or protect the other nation, where the armed attack has occurred, in collective defense. This right to self defense continues until the Security Council takes measures necessary to maintain peace and security. As opposed to the Article 42 of the UN Charter, *there is no need for a resolution* passed by the Security Council in Article 51 of the UN Charter to declare if the member nations have the right to individual or collective self-defense in the concrete cases. This is *fairly problematic*, because concrete cases can be interpreted in more ways.

Perhaps it is not an exaggeration to state that *the states interpret the provisions of the Article 51 of the UN Charter in the manner of their political goals* as it happened when the US and Great Britain attacked Iraq in 2006. It can be limited only by the resolution of the Security Council that declares a state as aggressor, for example Israel, when used the right of self-defense in response to the terrorist attacks of the Hamas. For example, the Article 51 of the UN Charter determines the right to self defense only if the *first armed attack* has occurred. *Anticipatory self-defense* has a wide interpretation of this provision of the UN Charter. It means that using military force to defeat the threat of an armed attack even before the first strike occurs can be justified on the basis of self-defense. The definition of armed attack has not been defined by the UN Charter, because after the 2nd World War it originally was modeled to the traditional warfare, which was fairly ambiguous. As mentioned earlier, it has become a vague area in the second part of the 20th century.

After the 9/11 terrorist attack, the Security Council passed the *Resolution 1368*, reflecting to the terrorist attack occurred in New York, Washington D.C and Pennsylvania on September 11, 2001. The Security Council declared the terrorist attack of 9/11 is a *threat to international peace and security*, and expressed that perpetrators, organizers and sponsors of this terrorist attack should urgently be brought to justice. This resolution also declared that those *responsible for aiding, supporting the perpetrators, organizers and sponsors*, will be held accountable. There have been *several interpretations* on the basis of Resolution 1368, which otherwise seems to be a declaration rather than a legal provision.

The first conclusion to be made on the interpretation of the Resolution 1368 is that terrorist attacks have been taken *under the force of the Article*

42 and Article 51. Based on these articles, the Security Council *authorized the member nations of the UN to use military force*, and at the same time declared the right of the nations to individual and collective self defense in response to the terrorist attack of 9/11. The Resolution 1368 makes it clear, too, that military force is allowed to use in the case of terrorist threat, but *does not specify when, where and how much force* may be used. The lack of such an interpretation is also problematic in the concrete cases. Israel for example, has regularly been attacked by the Hezbollah and the Hamas in the way of suicide bombing, explosion, taking of hostages and missiles. These are armed attacks, and terrorist attacks at the same time perpetrated by those terrorist groups that are strongly sponsored by the state.[3]

The Israeli state used military force against Gaza and Lebanon as sponsoring state, but it was not always supported by the Security Council. The reason expressed by the Security Council was that Israel used prohibited weapon, and *did not keep the principle of the proportionality* in its respond, for example killed civilians. The other side of the truth is that the Palestine combatants used human shields and put the military objectives in hospitals.

One thing seems to be sure on the basis of the Resolution 1368: terrorist attacks shall be under the force of the UN Charter. Further conclusion to be drawn is that not only the individuals and groups taking part in terrorist attacks should be responsible, but the *states, that sponsor the terrorist groups*, as well. The terrorist attack of 9/11 was evidently an international terrorist attack, perpetrated by the terrorist group, Al Qaeda, not the Afghan state. The US attacked the Afghan state, based on the Resolution 1361, which interpreted the Article 51 of the UN Charter in the way that the Afghanistan is a sponsoring state. President Bush gave Afghanistan an ultimatum to extradite Bin Laden otherwise the state will be attacked by the US military forces. It is obvious that the Afghan state was a sponsoring state, even if they would not have rejected the extradition of Bin Laden. That is, on the tribal areas of Afghanistan, which were uncontrolled by the state, the Al Qaeda had (and still has) terrorist training camps and other terrorist facilities.

Interpretation of Resolution 1361 *gave the right in this way to the US to use military force against Afghanistan*, however the terrorist attack of 9/11 was perpetrated by the Al Qaeda, not the Afghan state. The military force in the form of *targeted killing* used by the US *against Pakistan or Yemen*, for example, *cannot be justified* on the basis of such interpretation of the Resolution 1361. This is because it cannot be proved if these states in fact support terrorist groups in any way, or if so, they really want and are able to control the tribal areas. Regardless, neither of these states was directly involved in any armed attack or did not threaten or violate international peace and security in any way, which would serve as a base for

the use of force against them. When the US and Great Britain attacked Iraq, *it was not based on any resolution of the Security Council*. The Security Council passed two resolutions in 1998 and in 2002, in which declared that Iraq did not cooperate with the International Atomic Energy Agency, and obligates it to do so.

The US and Great Britain justified the starting war to Iraq in 2006 with the *right to self-defense*: they wanted to find the weapons of mass destruction and destroy them, capture the terrorists and assure that those who are in need can receive the humanitarian aids. They also referred to the fact that did not aim to violate its territorial integrity and political independency. This is, however an *extremely wide way of the interpretation* of the self-defense, because the Article 51 of the UN Charter can be applied only in the case of an *armed attack*, which did occur in any way from the side of Iraq.

The Resolution 1361 can be applied in the case, too, when a nation under terrorist attack *request the assistance* of other nation, and can be considered as collective self-defense. The incumbent government, as it happened in Mali, may ask another state to intervene, i.e. the government of Mali asked French government to help crush the insurgent group in the Northern part of the country.

These examples show *how widely* the right to use of armed forces can be interpreted in the practical reality, and *can adjust it to the actual political benefit* of the politically strongest states. The other question is when a state can use force in the case of insurgency, civil war, revolution, or military putsch which occurs *in the boundaries* of the given state. The state obviously has the right to regulate the use force in such cases in the constitution or in domestic acts, but it is queried in the international law, if other states or international organizations can intervene. These armed conflicts can easily lead to *undesirable effects*, such as illegal weapon trade, terrorism, wave of refugees, ethnic cleansing, etc., which threatens the international peace and security. The NATO air bombing, for example, was implemented in the former Yugoslavia in 1999 on the basis of the resolution of the Security Council, in which this was the reason for the intervention. The Syrian civil war has generated the same problems, like it was in Kosovo in 1999, but the Security Council has not achieved any decision until this time in the case.

Prohibited intervention is interpreted by the Security Council as the *intervention in the internal cases of the state*, for example, support of terrorism, insurgency or internal armed conflict in the form of weapon transport, military base, military advisers, etc. It has often happened during the last decades that terrorist groups, for example, the Al Qaeda and the Hezbollah intervened in Iraqi war and Syrian civil war, or Russia, too, with weapon transport to the Syrian civil war. As mentioned earlier, prohibited intervention cannot be punished in a direct way by

the international law, unless it jeopardizes the international peace and security based on the Article 42 of the UN Charter.

Intervention can be *indirect*, too, such as blockade, embargo, too, which can be lawful actions, in the case of threat to force and use of force. The Article 1 of the UN Charter determines as one of the aims of the United Nations to respect and promote human rights and fundamental freedom. *Violation of human rights* can also be a base of a lawful intervention, as mentioned earlier, if it is related to the international peace and security. According to the international legal practice, only the Security Council has the right to take actions in these cases. One of these actions is the *peace enforcement*, which means that the opposing parties of the civil war should be disarmed by using military force. This was the reason why the Security Council decided to use peace enforcement in Bosnia in 1992-95 and in Congo in 2003, for example. The international customary law acknowledges the right of the government to facing in internal armed conflict *to conduct military operations those citizens taking an active part in hostilities against the government*, in addition to law enforcement activities. This is the case when the armed conflict does not have any international character, as was examined earlier in this chapter.

7. Constitutional Rights vs. Efficiency Requirements

Counterinsurgency and counterterrorism require the so called *“comprehensive approach”* both on domestic and international level, which supposes military, intelligence, law enforcement, jurisdiction, and administrative means to be applied at the same time. *Efficiency requirements* can be guaranteed only in this way. There are, however, contradiction between efficiency requirements and the *traditional principles* of the Western democracy, such as the rule of law, constitutionalism, pluralism, human rights, freedom, openness, tolerance, etc. The Western countries try to balance between the *individual liberty* and *public safety* in their counterterrorism efforts. It should be noted that for the legislation of the EU only the Islam terrorism has any relevance, because local insurgencies or local terrorist groups have not existed anymore. As a reaction of the terrorist attacks in 2004 in Madrid and in 2005 in London, the European Union more intensively began to take part in counterinsurgency, and elaborated a *new strategy* to it. It is especially important for the legislation of the EU, because it should be in accordance with the basic principles and values of its charters.

Laws on the counterterrorism should be based on the requirements identified by the European Union public policy. These are as follows: quick, coherent, goal-oriented, cost-effective operations, and clear, unambiguous legal regulations. According to the *self-critic* of the European Union, the relevant legal

regulation is often not capable to follow efficiency requirements of the counterinsurgency, which led to inadequate and insufficient operations.

There have been two emerging issues in this field: *competence* of the international organizations vs. domestic public authorities, and the possible *limitation of the constitutional rights*. Regarding the former one, it is problematic, how to share the competence of intelligence on international and domestic level, such as collecting and analyzing data, law enforcement, immigration and border management, so that overlapping and the withdrawal of the competence of the member states can be avoided. It is still debated in the EU in what extend certain constitutional rights, such as right to privacy, ownership, fair jurisdiction, human dignity and freedom, can be limited so that efficiency requirements of the counterinsurgency can be achieved.

The EU Counter-terrorism strategy[6] determined four principles of counterterrorism:

- Prevention
- Protection
- Respond
- Pursue

8. Questions of Legitimacy and the Rule of Law in COIN

Counterinsurgency has been thought after the failures of the military engagements in the Iraqi and Afghan wars to be a more complex issue, i.e. an *integrated set of military, political, economic and social measures*, which aim to end the armed conflict, but instead, create and maintain a stable political, economic and social structures, and resolve the underlying causes of the insurgency. This is called as "*win the population strategy*".

The "win-the-population" strategy of the counterinsurgency aims to have the *support of the population*, and the incumbent government competes with the insurgent groups to reach this goal. The population will sympathize with the side that can offer better governance, i.e. security, welfare, economic development, rule of law, democratic elections, public safety, human rights, etc. *Legitimacy* forms an integral part of the "win-the-population" strategy. There have been several attempts in the military literature to determine the contents of this terminology. The *traditional meaning* of legitimacy in the political sciences is the origin of the political power of the state. According to the Western view, the precondition of the legitimacy is the democratic elections. The legitimacy in the theocratic states is based on the religion and is thought that the source of the political power should be the god, and the role of the government is to implement its will. Autocratic states are not considered as legitimate.

The meaning of the legitimacy *in the counterinsurgency* has been extended to as a system

of management means in the given situation of the counterinsurgency campaign. It has two parts: the security operation aims to minimize the armed conflict in the way of killing only the most fanatic leaders, giving amnesty to the insurgents, declaring ceasefire or armistice, etc.

The Iraqi security operation, called "Anbar Awakening" was successful, because the brutal terrorist attacks frightened the Sunni tribes away the Al Qaeda, and began to support the incumbent government. The Sunni tribes later were integrated in the police, and got amnesty. As a result, the number of the terrorist attacks dramatically decreased. Such a program was not successful in Afghanistan, where only the 3% of the Taliban wanted to join the government forces. The militias in Congo, for example, formed the part of state regular army after the militias had been crushed.

Detention policy of the counterinsurgency should help the host nation to develop their jurisdiction so that they can open a legal procedure against the criminals, but not to send them to the courts of other countries. When the host nation does not have sufficient jurisdiction, as it was the case in Iraq, or is reluctant to take the criminals to the trial, the International Criminal Court should proceed.

It is important during the security operations, when a foreign country or international organization implements it, to show that the country is *not occupied by the enemies*, but they help to establish security and basic public services. The other step of the counterinsurgency campaign is the *stability operation*. It aims to establish the *basic institutions of a well operating government*, such as legislation, public administration, jurisdiction, law enforcement, democratic voting system, social welfare system, infrastructure services, open media, etc. The *rule of law* has a great importance during the security and stability operations. The general constitutional interpretation of the rule of law outlines security, predictability and lawfulness. The *military doctrine of the rule of law* in the counterinsurgency campaign covers *concrete legal requirements*, such as accountability to laws, supremacy of law, equality before the law, fairness in applying law, access to law, separation of power, participation of the population in decision making, procedural and legal transparency, state monopoly in the use of force and resolution of disputes, stable law, etc.

The rule of law is also related to the question of "*reciprocity*" or "*exemplarism*", which means two options for the counterinsurgency to choose: the reaction to the criminal actions of the insurgents will be reprisal with unlawful engagements, or to respect the rule of law, even if the insurgents do not do so. No doubt that the latter one will succeed in the long term, because of the support of the population. Application of the rule of law is especially important, when the incumbent government establishes *jurisdiction*, because some efficiency requirements

can be assured only in this way. For example, if the criminals of the insurgency will not be taken to the court, punished in a brutal way, executed without judgment of the court, tortured, humiliated, etc., the stability operation will lose its legitimacy in the eye of the population. *Efficient legislation* can be guaranteed only by the use of the rule of law, because only the rule of law can achieve the principles of the democracy, such as participation in the decision-making process, free elections, transparency, integrity, accountability, etc. which are the guarantee to avoid development of dictatorship.

We have to emphasize, however, that the aim of the counterinsurgency campaign is not to establish a *western-type democracy*, but a government that can provide the basic state functions with taking into account the *local traditions*, as well. For example, most of the Muslim countries would reject the equality of the women and ethnic minorities, or the legislation and jurisdiction are often based on the Islam. The incumbent government in Afghanistan established a court-system, as a part of the state power, but the population did not rely on it, much better the “jirga”, the tribal council that decides in legal disputes, and has a legislative function, as well. During the way from the “kill and capture” strategy toward the “win-the-population” strategy the incumbent government has to face certain legal problems.

The *targeted killing* is used against the leaders of the terrorist and insurgent groups in the form of combat drones, air bombings, special operations, intelligence, because otherwise it would be impossible to capture them. They can often successfully hide in the population, e.g. terrorists on the tribal areas of Afghanistan and Pakistan that are not controlled by the state, or in the high hills, e.g. Tora Bora in Afghanistan, or on the desert. Neither law enforcement, nor traditional military engagement will be a sufficient means to capture them.

Targeted killing, however it is a highly sufficient means with a great political benefit, e.g. liquidating of Bin Laden, is still an unlawful action, unless it should be considered as a military use of force authorized by the Security Council, or based on self-defense. This is because even if these leaders are not under the force of the law of war and humanitarian treatment, they have human rights that cannot be violated in any way. Targeted killing is against certain human rights, such as the right to life and fair jurisdiction. Furthermore, it occurs fairly frequently that *civilians* are also attacked in targeted killing.

This has been debated even in the military doctrines in which situation civilians can be attacked. As mentioned earlier, the European Court on Human Rights elaborated its interpretation for such cases, which hardly can be applied in the practical reality. According to the American approach, to be the member of the war-fighting apparatus is enough for

the military forces to attack them, but the opinion of the Red Cross is that direct causal relationship is needed for the combatants to attack. In most cases of the targeted killing it is, however, almost impossible to separate civilians from the terrorists, especially in crowd, bombing, or buildings. It is a custom, for example in Afghanistan that the guests shoot at the weddings in the air, which can be mixed with attacking combatants. The drone combatants, special operations, and the air bombings cannot be targeted only to terrorist persons, as opposed to “traditional” liquidations implemented by the intelligence agencies. It has become a practice of the warfare that civilians killed and injured in targeted killings will be compensated by the government of the military forces that is responsible for the targeted killing.

Targeted killing is a best example for the *dilemma* whether to prefer efficiency of the military engagement or respect the laws on war. From legal point of view, this problem seems to be unresolved. Many lawyers suggest for the armies to introduce non-lethal weapons, such as directed energy beams, malodorants, calmatives, etc. in these cases. These kinds of weapons can incapacitate persons, while minimizing fatalities and injuries.

Conclusions

A general conclusion can be drawn based on this study that recent international law on warfare cannot sufficiently be applied in the practical reality. The reason is that warfare has changed a lot during the last decades, in other words, traditional symmetric warfare has increasingly been replaced by new forms of asymmetric one, such as terrorism and insurgency. Further problem we have to face to is that if terrorism, which is typified in most cases as a clandestine non-state actor with international character, connected occasionally to state authorities or directly supported by the state, should be considered as a criminal issue, even if terrorist groups are similar in their methods to warfare. Counterterrorism, that is, often requires military engagements, too, besides law enforcement, so that it should be efficient. International law is fairly contradictory when on one hand refers to terrorist groups as subject to criminal law of the domestic laws, which seems to be increasingly insufficient in concrete cases, but does not admit the right of use of force based on the law on warfare on the other hand, even if use of military force has been required.

There have happened important efforts in establishing cooperation among the states in the counterterrorism in the field of criminal law, such as prosecution, investigation, trial, or punishment, and administrative law, too, such as cross border management, border checking, immigration, etc. These new forms of counterterrorism, however, can be successful, only if terrorist attacks occur in the areas of the Western countries. Not insurgency, just

terrorism has been typical in these countries. Criminal law regulating warfare has had an increasingly international character, which means on the other hand, that it is going to be less and less subject to domestic monopoly. The International Criminal Court and the ad hoc criminal courts have already had a great relevance in this matter. Terrorism and insurgency in the Muslim countries arises other problems, than in the Western countries. Failed states, or those that cannot effectively control some of their areas, have been a hotbed of terrorism and insurgency. Neither of them can be defeated with pure criminal means.

Military engagements by the incumbent government against terrorism and insurgency is normally allowed, because domestic laws entitle the government to do so, but it is quite problematic in the international law, when other states and international organizations, such as the UN, the NATO or the EU, can intervene in the states struggling with terrorism and insurgency. The case, when the incumbent government cannot cope, or is unwilling either, with the problem of terrorism or insurgency, and intervention of other state has become necessary, is a vague issue. Terrorism vs. insurgency cannot be differentiated in neither the military sciences, nor the military practice, due to overlapping. Terrorism has greatly been interwoven with the insurgent groups, or the supporting states, and insurgent groups often have a double character: guerilla warfare and terrorist attacks at the same time, furthermore in many cases both of them are related to the organized crime.

International law, respecting the principles of national sovereignty and non-intervention, admit the right to use of force against other countries only in exceptional cases, i.e. in self-defense or if the Security Council decides so, based on the violation of international peace and security. It is not an exaggeration to state that state-intervention in such situations has been subject to political issues rather than that of international law. This is because the provisions of the latter one can be interpreted in many ways, due to its generally formulated legal norms, and also, the politically dominated character of the Security Council.

Further problem with the international legal regulation on the warfare is that it cannot make difference between terrorism and insurgency due to the lack of any legal definition. Laws, instead, make distinction on that basis if the armed conflict has occurred between regular armies, or not, or if it has a war character. Terrorism and insurgency in our days just rarely operate in this traditional way, but have special features. It is also problematic in the international law on the warfare that it cannot make difference between terrorism and insurgency in the lack of sufficient legal definition. Laws, instead, make distinction on the basis if the armed conflict has occurred between regular armies or not, or has a war character. Terrorism and insurgency in our days just

rarely operate in this traditional way, but have special features.

When special military engagements, such as targeted killing, use of special force, liquidations, intelligence, etc. should be implemented in the counterterrorism and counterinsurgency, it cannot be decided in the concrete cases, as to whether the law on warfare, i.e. Hague Conventions and Geneva Conventions shall be applied or not. It would be especially important to make clear if these military forces have to respect these laws on warfare, or not, both to in their relations with the enemies and civilians.

In the lack of sufficient regulations of the international laws, human rights will be applied in these military engagements. Human rights, however, are not the best legal institutions to make sufficient legal decisions in military issues. For example, it cannot be answered clearly, based on human rights, when civilians and civil objects can be attacked by the military forces, which is a most emerging issue of counterinsurgency and counterterrorism.

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PUBLIC PROCUREMENT IN ZIMBABWE: ISSUES AND CHALLENGES

*Daniel Chigudu **

Abstract

With negative coverage largely by the media on state procurement, this article aims at exploring challenges and issues that militate against public procurement in Zimbabwe. The exploration is done through content analysis of statutes and procurement practices that currently obtain in the country. The study shows that despite the presence of some regulations public officials manipulate tender procedures for personal gains. There is need for improved political will to enforce the law on errant behavior. The value for money that the procurement system should promote is lost. There is no mechanism for feedback to inform management and policy makers. The article provides recommendations for the government in pursuit of public procurement best practices. **

Keywords: Public Procurement, Public Officials, Tender Procedures

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1. Introduction

Public and political expectations for effective service delivery put public procurement under intense scrutiny (Bolton, 2006). Public procurement is an activity of purchasing the goods and services which a government needs to carry out its functions. Other scholars use different terminology to mean the same concept. The World Trade Organisation (WTO) uses the term government procurement and the United States uses the term public contracts or government contracts.

Public procurement is central to government service delivery as it often involves large sums of money. The Organisation for European Co-operation and Development (OECD) has estimated that public procurement can account for up to 5% of gross domestic product in developing countries and averages about 20% of public expenditure. According to Callender and Mathews (2000) public procurement officials around the globe control spending that is equivalent to 10% to 30% of GNP in any given year. It is therefore imperative that, procurement systems should be transparent and high performing in order to guarantee cost-effective delivery of goods and services. A research carried by Musanzikwa (2013) reports that, procurement expenditure constitutes over 65% of total public sector expenditure. Central government purchases range from 9% to 13% in the Middle East and Africa and this indicates that public procurement in a country plays a vital role (Odhiambo and Kamau, 2003:10). Ambe and

Badenhorst-Weiss (2012:245) note that, public procurement plays a key role in the successful management of resources and is increasingly getting recognised as a profession.

In Zimbabwe, public procurement is dominated by procedures and guidelines meant to ensure a fair process that provide value for money. In real practice, these guidelines tend to provide opportunities for abuse and malpractice for some procurement officials. Constitution amendment number 20, section 315 makes provision for the public procurement in general. Procurement Act (chapter 22:14) gives more details about functions, appointment and disqualification of members that constitute the State Procurement Board (SPB). This article discusses the research method used and reviews the nature of public procurement and its origin. It discusses public procurement in Zimbabwe and the legislative framework that is in place.

The article also highlights major issues reported by the print media and constraints to effective and efficient implementation of public procurement in Zimbabwe. Recommendations for the way forward are given that suit the economic environment of the country.

2. Research Method

Being exploratory in nature, this article employs a content analysis / conceptual analytical approach to research. According to Funer (2004), in conceptual analysis, concepts are treated as classes of objects,

relationships, properties or events. This involves definition of the concept through identifying and specifying the conditions under which the phenomenon is classified or could be classified. It is used to get an in-depth understanding of public procurement practices in Zimbabwe. The study benefits from content analysis of the provisions and guidelines of procurement as outlined in the Administrative Justice Act (chapter 10:28); Competition Act (chapter 14:28) and the Procurement Act (chapter 22:14). This will be complemented by data from secondary sources including but not limited to research reports and relevant literature review.

3. An Overview of Public Procurement

Arrowsmith (2010) defines public procurement as the government's activity of purchasing goods and services needed to perform its functions. It refers to procurement planning, contract placement and contract administration. The history of public procurement dates back to 800B.C in the development of silk trade between China and a Greek colony as noted by Thai (2001). According to Coe (1989; 87), there is evidence of the earliest procurement order inscribed on a red clay tablet found in Syria with order dates between 2400 and 2800B.C being for "50 jars of fragrant smooth oil for small weight in grain".

Page (1980) reports that, in the United States of America, government procurement in municipalities predates that of state and federal governments and there were no procurement officials. The state legislatures began to create boards or bureaus responsible for purchasing in the late 1800s. Centralised purchasing gradually became common in local government and state. In recent years, researchers and practitioners have argued that purchasing in government must be centralised in order to provide more responsive support to end users especially in government. This eliminates bureaucratic obstacles, improve inter-departmental coordination and empower service delivery managers to procure without impediments by a centralised entity (Thai, 2001). However, despite many government procurement reforms in the United States over eighty years ago (Thomas, 1919:5), it appears problems are still similar today and may persist forever as a result of lasting unfavourable public perceptions. The problems are stated below:

Governments have in the past with few exceptions notoriously failed as purchasers. Dealers complain of red tape which hampers them in bidding, in delivering goods and in securing the payment of bills. Government executives themselves complain of delays between the issue of purchase acquisitions and the availability of goods for use. Citizens generally are prone to assert that graft and political favouritism taint a large part of government purchasing.

While Arrowsmith(1998) noted that, public procurement has been utilised as an important tool for achieving social, economic and other objectives, some have perceived public procurement as an area of waste and corruption(Thai,2001). According to Transparency International (undated, chapter 2);

Mention the subject of corruption in government and most people will immediately think of bribes paid or received for the award of contracts for goods or services, or –to use the technical term –procurement. Whether this is really the most common form of public corruption may be questionable but without doubt it is alarmingly widespread and almost certainly the most publicised. Hardly a day goes by without the revelation of another major scandal in public procurement somewhere in the world.

Surveys conducted in 1995 by Transparency International (TI)'s national chapters reveal that corruption in the public sector manifests in much the same forms whether in developing countries or developed ones. The areas most vulnerable to corruption include, re-zoning of land .government appointments, and public procurement (Transparency international, undated).In view of this, in South Africa's Constitution section 187 makes the following procurement provisions;

- The procurement of goods and services for any level of government shall be regulated by an Act of parliament and provincial laws, which shall make provision for the appointment of independent and impartial tender boards to deal with such procurements.
- The tendering system referred to in subsection (1) shall be fair, public and competitive, and tender boards shall on request give reasons for their decisions to interested parties.
- No organ of state and no member of any organ of state or any other person shall improperly interfere with the decisions and operations of the tender board.

All decisions of any tender board shall be recorded.

Sources of procurement regulations in most countries include statutes passed by legislative bodies, national constitutions, executive orders issued by chief executives or their delegates, rules and regulations and administrative law decisions. Thai (2001) contends that, public procurement is a very complicated system in which there are many conflicting interests. As such, sound procurement regulations are needed to increase public confidence in the procedures and to ensure fair treatment of all participants who deal with the system. The procurement systems must provide feedback to policy makers and management so that they are made aware of procurement problems that the public procurement system encounters.

4. The Public Procurement System and its Environment

The environment which influences the public procurement system like any other system include, the legal ,political ,market, internal and socio-economic environment.

4.1. Internal environment

This involves professionalism and procurement related workforce and the interactions between the three branches of government

4.2. Market environment

Due to variations in economic growth among countries, market conditions are favourable in developed countries and may not be favourable in developing countries. The National Institute of Governmental Purchasing (1999:34) reported that, “before embarking on a foreign purchasing program, public procurement professionals must carefully assess the total cost implications and compare them to domestic cost.” Professionals in public procurement are often torn between their countries’ economic development policies and free trade agreements when they face a hard choice of selecting between foreign and domestic firms (Thai;2001).

4.3. Legal environment

As opposed to public procurement rules and regulations, the legal environment refers to broader legal framework that governs business activities. These include among others; regulations dealing with equal opportunities for the minorities and women, disclosure of product characteristics, deception of advertising, disclosure of information, workplace and pollution control, health and safety, manufacturing and marketing, contract law and disputes.

4.4. Political environment

In a democracy, interest groups are actively involved in aspects of public procurement systems. They lobby legislative bodies to alter or pass statutes. What normally sees the light of the day is a compromise between government and interest groups.

4.5. Socio- economic environment

Most countries prefer national or local firms over firms from other countries. Professionals in public procurement may be in an unfavourable or favourable environment that has a great impact on their practices as they face imperfect competitive markets. Culture and technology also influence public procurement. Where giving gifts is a common public relation

practice in a given culture, it may be difficult to make a distinction between gifts and bribes.

The World Bank conducted a Country Procurement Assessment Review (CPAR) in collaboration with the government of Gambia and concluded that the country lacked four basic elements to have a good procurement system. These elements were;

- An adequate set of policies and procedures;
- A strong and effective procurement organisation;
- A sufficient number of competent and dedicated procurement staff;and
- An overseer and adjudicator to assure compliance.

Gambia may not be alone in lacking these four elements.

After the overview above, the discussion proceeds to public procurement in Zimbabwe’s public sector.

5. Management of Public Procurement

There are two key pieces of legislation that guide management of public institutions in procurement. These are, the Administrative Justice Act (Chapter 10:28) and the Competition Act (Chapter 14:28).The Administrative Justice Act is primarily concerned with procedural aspects of procurement while the Competition Act focuses more on promoting competitive procurement. While public sector organisations have internal regulations that direct the procurement process such regulations are not expected to conflict with Acts of Parliament.

Chikomwe (2012) reminds public entities when he refers to the Administrative Justice Act section 3 which requires administrative authorities to act lawfully, reasonably, fairly and to supply written reasons for awarding a tender and section 5 which deals with the basis upon which non-compliance with section 3 is determined. He argues that, a basic procurement process in Zimbabwe must have the following identifiable components; pre-qualification, anti-fraud/corruption declarations, qualification criteria, eligibility, bid preparation, bid submission, notification, adjudication and award criteria.

In pre-qualification, the tender process certifies genuine applicants as ones registered with the State Procurement Board of Zimbabwe (SPB).These applicants are expected to reveal their compliance with statutory obligations to remit corporate tax to the Zimbabwe Revenue Authority (ZIMRA).When they append their signatures to the anti-fraud declaration paper, bidders undertake not to flout the procurement procedures like dangling inducements to members of the procurement committee. By appending their signatures they also agree to be punished in the event that a fraudulent activity is proved against them. The qualification criteria assess the potential capacity of

the prospective supplier to deliver goods or services in a timely manner and the litigation history if any.

6. The Legal Framework

The main legal texts for public procurement in Zimbabwe are:

- The Constitution of Zimbabwe (Amendment No: 20 Of 2013).
- The Procurement Act (2 of 1999).
- The Procurement Regulations, (2002).
- The Procurement (Amendment) Regulations, 2003 No.2.
- Urban Councils Act of 1995 (revised 1996).

7. The State Procurement Board of Zimbabwe

The State Procurement Board is an institution that is empowered by the Procurement Act to conduct procurement on behalf of procuring entities where the procurement is of a class prescribed in procurement regulation. The institution supervises procurement proceedings conducted by procuring entities in order to ensure compliance with the Act. If there is suspicion of malpractice or allegations raised against a procuring entity the State Procurement Board initiates investigations and takes action as provided in Section 47. As far as possible, the SPB is not subject to the direction or control of any person or authority in the exercise of its function according to the Procurement Act.

8. Procurement, Tendering and Regulatory Issues

The procuring entity is obliged to float tenders for goods and construction works to be done. The method of procurement should be according to the provisions of section 32. If for some reason a method adopted is not provided for a record of the circumstances which justify adoption of the method should be clearly stated. In undertaking the tender, invitation to suppliers should be published in newspapers that circulate in the area. But, if the procuring entity is the state then publication is done in the government gazette. For tenders extended to non-nationals the publications should be made through international newspapers or professional journals especially for services that are highly technical in nature. Basic information that should be carried in the invitation to suppliers includes the procuring entity's name and address; description of goods to be supplied and time within which the goods or services should be supplied. According to section 34; criteria by which suppliers will be evaluated should be given, manner in which solicitation documents may be obtained and their price, deadline for the submission of tenders and any relevant information.

The price for solicitation and pre-qualification documents should not exceed the cost of printing and providing them to the suppliers. The procuring entity must ensure that solicitation documents are detailed enough to solicit required information such as the criteria and procedure by which the successful tender will be determined. All requirements must apply to all suppliers and no tender should be disclosed to any other supplier. This means all tenders must be submitted in sealed envelopes and deposited in the tender box. All suppliers that submitted tenders should be permitted to witness the opening of the tenders and have the right to be informed of the price and other important terms of each tender opened. Finally, any formalities that need to be complied with are communicated to the successful tenderer before the procurement contract is concluded.

The procedure for procurement of services follows almost the same for tendering proceedings in terms of transparency and clarity. The procurement regulations are provided in Chapter 33 of the Act. The regulations are very clear on methods of procurement that may be adopted, classes of procurement, the manner in which suppliers should conduct themselves and alterations that suppliers may be permitted to make. There are provisions for circumstances in which the regulations may be departed from or waived. These may prescribe requirements by reference to the UNCITRAL Model Law on Procurement of Goods, Constructions and Services adopted by the United Nations Commission on International Trade Law at its 26th session in 1993.

With respect to eligibility, this is where most procuring entities falter. Section 34(1) (a) states clearly that suppliers must satisfy that, "...they possess the necessary professional and technical qualifications and competences, financial resources, equipment, facilities, personnel and experience to perform the procurement contract". It is easy to determine suppliers who were awarded tenders through bribes or corruption when measured against this clause.

9. Public Procurement Challenges in Zimbabwe

The print media has been awash with reports of corruption and bribes in the public procurement. Some matters have gone unreported despite having been unearthed by the internal or external auditors. While the rules and regulations on public procurement attempt to plug loopholes for corrupt practices there seem to be no enabling legal framework to allow bidder's enforceable right to review when public entities breach the rules. The statutes are clear on the oversight role of the State Procurement Board on procuring entities but it appears the law is silent on who oversees the State Procurement Board itself.

Literature has shown that, the most successful procurement systems are those that provide bidders a legal basis to challenge the actions of public procurement officials when they breach rules (Hunja, 2001). For this reason, the World Bank regularly carries out assessments of procurement systems. It does carry these assessments in the countries where it lends, aimed at identifying strengths and weaknesses of the entire public procurement sector. It is also for this reason why the United Nations Commission on International Trade Law (UNCITRAL) also carried out a study of procurement laws in many developing countries. Like in Zimbabwe, Hunja (2001) argues that one consistent weakness in most developing countries appears to be the lack of an entity within government that is charged with overall responsibility to ensure that the system is properly functioning. He contends that the lack of an entity that has oversight responsibilities creates serious gaps in the enforcement of rules and regulations. In Zimbabwe, the most difficult challenge to install such an oversight body may be the lack of political will at the highest levels of government to significantly overhaul the existing system and capacitate the Anti-Corruption Commission. Some of the most apparent challenges are highlighted below.

9.1 Lack of political will and vested interests

Vested interests can manifest themselves through local business cartels in which the private sector and their collaborators in the public institutions benefit from such flawed systems. Where a procurement system is loose, there are opportunities for abuse of the tender process through patronage and corruption. Hunja observed that access to public contracts in developing countries serves as a means in most cases of financing political parties and to reward political party supporters. In the absence of political will, recommendations can be made, draft laws discussed and position papers made but no action may be made to implement changes proposed.

9.2 Lack of knowledge and capacity

Although Zimbabwe appears to have some modern legal public procurement frameworks, some political bureaucrats may lack the knowledge of good procurement practices and procedures and yet occupying influential positions in the procuring entities.

9.3 Type of legal instrument

Scholars have observed that common law countries which have inherited a procurement system based on the United Kingdom (UK) model like Zimbabwe, it is the type of juridical instrument that the reforms should put in place to regulate public procurement.

The UK historically, regulated public procurement by means of a set of regulations. While this has changed with most of the procurement in UK being governed by the European Union Directives on Procurement, most developing countries that have the UK based model such as Zimbabwe, have maintained this basic structure. This has proven to be problematic because such regulations apply mainly to central government. This leaves local authorities and state owned enterprises to create their own systems of procurement.

9.4 Legal enforcement

In Zimbabwe, the flagrant abuse of the procurement system is largely due to the fact that there is hardly any consistent enforcement of the rules and regulations. The procurement entities pretend to comply with procurement procedures while in actual fact compromising the spirit of the rules. The public officials and their accomplices severely compromise the systems because they have no fear of retribution if ever it comes. What is prevalent is advertising bids for a very short time so that just a few potential bidders get the opportunity and this reduces competition against their favourites who might have known about the coming advert well in advance. Uromo (2014) observes that despite, the fact that conflict of interest is covered under law, the law is not enforced in practice. For that reason, public officials still award tenders to themselves through a third party. In some cases, they award contracts to companies that are non-existent.

9.5 Indigenisation policy

The study by Musanzikwa (2013) revealed that the need to comply with the indigenization policy resulted in tenders being awarded to incompetent companies.

10. The Way Forward for Public Procurement in Zimbabwe

- Government should create tight procurement oversight mechanism on departmental procuring entities and the State Procurement Board
- Stakeholders must be educated on the value for money concept underlying public procurement systems so that they can report any form of graft.
- Alleged cases of public procurement must be thoroughly investigated and culprits brought to book with deterrent punitive measures taken
- Politicians must protect national resources rather than become accomplices of plundering
- Public officials involved in procurement must be trained adequately so that they carry their mandate efficiently and effectively.

- Losing tenderers must be given opportunities to learn how they missed the opportunity so that meaningful competition is encouraged in the next bidding in promotion of the value for money.
- The procurement system should provide a fair opportunity to all prospective suppliers of goods and services.
- Additional goods, works or services must be procured from the same source for reasons of standardization or compatibility with existing items
- Procurement should be free from political interference
- Suppliers who shortchange the procurement system must be debarred and blacklisted.
- There should be a board of contract appeals to resolve contract disputes between contract officers and contractors
- Feedback mechanisms should be put in place so that policy makers and management become aware of procurement problems the public procurement system may be encountering.
- Government must consider opening whistle blower channels
- Conflict of interest policies and fraud awareness training
- There should be policies setting out procedures and guidelines for giving and receiving gifts.

Conclusion

Given the economic status of Zimbabwe, it is prudent that public procurement be done fairly, transparently and realise the value for money. In the framework of content analysis, an examination of relevant literature and public procurement practices in Zimbabwe discussed, the challenges being faced are not insurmountable. Politicians and public officials need to reflect seriously on the recommendations and go to the drawing board to counter these challenges. The recommendations highlighted have worked in some developed countries and appear to be working in other developing countries in Africa. Dealing decisively with public procurement practitioners found guilty of flouting procurement procedures may go a long way to restore confidence in the public sector and help woo investors.

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FINANCIAL STATEMENTS AND THE DISCHARGING OF FINANCIAL ACCOUNTABILITY OF ORDINARY PUBLIC SCHOOLS IN SOUTH AFRICA

Frank Doussy *, Elza Doussy**

Abstract

The Schools Act, 84 of 1996 (section 42(b)), requires that all public schools in South Africa, “as soon as practical, but not later than three months after the end of each financial year, draw up annual financial statements”. These schools must further submit audited financial statements to the Department of Education within six months after the school’s year end (section 43) and according to section 43(6), “at the request of an interested person, the governing body must make the records referred to in section 42, and the audited or examined financial statements referred to in this section, available for inspection”. The compilation, auditing and submission of these statements are therefore legally required and are compulsory for all schools.

The study aims firstly to establish whether schools in South Africa comply with the current legislative prescripts and accounting and auditing practices, and secondly to identify possible problem areas in this regard.

Keywords: Financial Accountability, Financial Reporting, Financial Statements, Scarce Resources

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Introduction

The Schools Act, 84 of 1996 (hereafter SASA) in section 42(b), requires that all schools in South Africa, must “as soon as practical, but not later than three months after the end of each financial year, draw up annual financial statements”. These financial statements must be audited and submitted to the Department of Education within six months after the school’s year end. Furthermore, according to section 43(6), the governing body of a school must make these audited financial statements available for inspection at the request of “an interested person”. The availability, compilation, auditing and submission of these statements are therefore legally required and are compulsory for all schools. (Republic of South Africa, 1996).

This paper explores firstly the availability of financial statements of South African schools and secondly analyses the contents of the financial statements of four ordinary South African schools to judge the quality and consistency of compliance with legal requirements and accounting and auditing practices.

Aim and importance of the study

The study aims firstly to establish whether schools in South Africa comply with the current legislative prescripts and accounting and auditing practices, and secondly to identify possible problem areas in this regard.

The study should contribute to the information database on financial matters of schools and could provide information about the value of financial statements regarding the discharge of financial accountability in schools. This information could help improve public trust in the South African school system and could help the Education Departments to evaluate the financial management and performance of schools. Improved information could lead to improved policies and regulation.

The results could also inform the accounting and auditing professions about the adequacy of the current system of drafting and/or auditing the annual financial statements of schools.

Limitations of the study

This is an exploratory study of the financial statements of only four schools and therefore the conclusions cannot be extrapolated to all schools in South Africa. Financial statements alone can also not

provide all the information necessary to discharge financial accountability. Furthermore, one should realise that there are limitations to the information presented in financial statements. Because of the accounting practices that have become generally accepted, subjective qualitative factors, current values, the impact of inflation and opportunity cost are not usually reflected in financial statements. In addition, many financial statement amounts involve estimates and because of permissible alternative accounting practices, comparisons between different entities may not always be appropriate. (Koen and Oberholzer, 2002:9-10).

Background

Education is one of the most important services provided by governments world-wide and this is also true for South Africa. According to South Africa Government online (2014), spending on education will reach R236 billion in 2014/2015. Schools, undoubtedly, form the foundation of the entire education system, with 25 826 ordinary schools in South Africa in 2012. (Department of Basic Education, 2014).

Public schools in South Africa receive funding from the respective provincial departments of education under which they fall. This money is derived from taxes paid by the public. Schools also receive further funds from a variety of sources like parents and other private individuals and/or institutions. Schools have a responsibility to use this money effectively to provide quality education and have to be able to demonstrate that they have done so. One way of providing evidence of how a school has managed their finances is by compiling financial reports. These reports include but are not limited to, annual financial statements. However, annual financial statements are the most widely used and most comprehensive way of communicating financial information about an entity, especially to external users (Shim 2008:15).

The South African education has in recent years been decentralised in an attempt to ensure quality education through the participation of parents and communities in the governance of their children's schools. Such sharing of power is in line with international trends as well as South Africa's constitutional imperative of democratic governance. For this potential to be realised, parents and community members need access to information about the school's performance. The increased school autonomy places a stronger demand on accountability as schools with more decision-making powers are required to account for their decisions and the impact thereof.

The term "accountability" is commonly found in modern public administration theory and practice and is defined as the fact or condition of being "accountable". The Institute for Accountability in

Southern Africa (IFAISA), defines accountability as the "obligation of those with power to explain their performance and justify their decisions" (IFAISA, 2014). The BusinessDictionary.com (2014), defines accountability as "the obligation of an individual or organization to account for its activities, accept responsibility for them, and to disclose the results in a transparent manner". Basically, accountability derives from the practical need to delegate certain tasks to others (agents). Those entrusted with these delegated duties are responsible for performing these actions in such a manner as can be reasonably expected under the relevant conditions. It is also expected that they render an account of their actions.

Evidence from the literature emphasises that accountability is made up of two parts, "the element of account" and the "holding to account". Rendering an account involves reporting and explaining or justifying the occurrence of activities (Wagner, 1989:7 - 16; Law, 1999:78-97). This involves providing information (i.e. reporting) to other people voluntarily or compulsorily (Maile, 2002). The second part, namely the holding to account, refers to parties to whom the "account" is given, the evaluation of the information provided, and the actions taken when after evaluating the information, a performance is found to be lacking according to some standard or expectation (Wagner, 1989:7-16; Law, 1999:80).

Accountability is clearly quite complex and dynamic and every accountability relationship implies the existence of a certain social framework, which will define the accountability relations (Rabrenović, 2009). It is not only a means through which individuals and organisations are held responsible for their actions (e.g. through legal obligations and explicit reporting and disclosure requirements), but also as a way for taking internal responsibility for shaping organisational mission and values, for opening entities to public or external scrutiny and for assessing performance in relation to goals. According to Ebrahim (2003), accountability operates along multiple levels – involving numerous actors (patrons, clients, selves), using various mechanisms and standards of performance (external and internal, explicit and implicit, legal and voluntary) and requiring various levels of organisational response (functional and strategic).

Accountability in an educational environment like a school also has many dimensions. Andersson (2005) describes three main types of accountability dimensions in education, namely: compliance with regulations, adherence to professional norms, and results driven accountability. Aucoin and Heintzman (2000:45), describe the accountability in a school as serving three purposes. The first is to control the abuse and misuse of public authority. The second is to provide assurance in respect of the use of public resources and adherence to the law and public service values. The third purpose is to encourage and

promote learning in pursuit of continuous improvement in governance and public management. Whittaker (1989:24) defines accountability in a school context as "...The duty or obligation of those given responsibilities and resources to explain and justify how they have used (or applied) the responsibility and resources in the achievement of agreed objectives. Whittaker (1989) stresses that this obligation is not only to "corporate entities, remote educational experts, or some restless national audience created by mass media, but rather to their local communities".

Financial accountability in a school is about assuring its stakeholders regarding the use of public resources (stewardship) as well as to underpin decision-making about how to allocate scarce resources like time, personnel, space, equipment and money. The allocation of resources may affect learner success (Xaba and Ngubane, 2010) and therefore the entire operation and success of a school often hinges on the quality of its financial management. It is therefore clear that a school has to provide information about financial activities to its stakeholders in order to discharge financial accountability.

The South African Schools Act renders the school governing body (SGB) responsible for the management of the school, including the financial management (Mestry, 2004; 2013). As elected officials, the SGB must demonstrate financial accountability for their performance to the different stakeholders to assure them that the funds entrusted to the school are being used to optimise the educational experiences of learners (Joubert, 2006; Joubert and Bray, 2007:28; Mbatsane, 2006; Mestry, 2004).

Demonstrating financial accountability can take many forms but essentially refers to the providing of financial information to stakeholders. The day-to-day financial operations and activities in any entity are usually too numerous to be reported individually to outsiders. The accounting system provides a mechanism to select, measure, and aggregate or summarise the financial activities for a specific time period into a variety of financial reports, including financial statements (Palepu and Healy, 2008: 1-4). A school's financial statements will therefore provide evidence of the school's financial operations and the management thereof.

The purpose of annual financial statements is to provide financial information to the governing body, parents, and other interested parties and as such, these statements form the basis of the governing body's responsibility to the community (in other words, accountability).

It is therefore no surprise that SASA, section 42(b) requires that all public schools in South Africa, must prepare annual financial statements. If the information is to be relevant it must be received on a timely basis and therefore a time limit is also specified. The statements must be prepared as soon as

practical, but not later than three months after the end of each financial year. Section 43 of this Act further requires that all public schools in South Africa submit audited financial statements to the Department of Education within six months after the school's year end. Furthermore, a school's financial records and financial statements must be made available for inspection by any interested person if so requested as per section 43. (Republic of South Africa, 1996).

The availability, compilation, auditing and submission of financial statements are therefore legally required and are compulsory for all schools.

Several authors have addressed financial management and financial accountability in South African schools (Bischoff, 1997:26; Joubert, 2006; Mbatsane, 2006; Mestry, 2004; Mestry, 2006; Ngubane, 2009; Xaba and Ngubane, 2010), but very few have commented specifically on the role of financial statements in this regard. However, both Mngoma (2009) and Makrweide (2012) highlight specific areas of concern.

Although the Accounting Officer's Guide (Republic of South Africa, 2000:19) states that financial information has no intrinsic value, but must be used by managers to develop plans, evaluate alternative courses of action and institute corrective action when necessary, the literature indicates that this aspect may be lacking in South Africa. Mahlane (2007) reports that in the Mopani District of the Limpopo Province, the majority of schools do submit audited reports, but apparently these reports are not assessed by the Education Department. Griesel (2011:360) gives a similar report. This does not seem to be unique to South Africa as Tooley and Guthrie (2007) report that schools in New Zealand also receive no feedback on annual reports submitted to the Ministry of Education.

No South African study analysing or assessing the contents of financial statements of schools could be found although Xaba and Ngubane (2010) as well as Doussy and Doussy (2012) recognise the importance thereof regarding accountability.

Quality of financial reporting

Over the years, the accounting profession through oversight bodies, developed certain international rules and guidelines on how financial information is treated and communicated. This ensures that measurement and presentation are less subjective (Elliot and Elliot, 2012: 212). These guidelines and rules for preparing financial statements are commonly known as Generally Accepted Accounting Principles (GAAP). In an attempt to set one international standard, the International Accounting Standards Board (IASB) issues International Accounting Standards (IASs) and International Financial Reporting Standards (IFRSs). These standards start with a conceptual framework which anchors financial reports to a set of principles such as materiality (the degree to which the

transaction is big enough to matter) and verifiability (the degree to which different people agree on how to measure the transaction). The standards establish which resources and obligations should be recorded as assets and liabilities, which changes in assets and liabilities should be recorded, when these changes should be recorded, how the recorded assets and liabilities and changes in them should be measured, what information should be disclosed and which financial statements should be prepared. In other words, the standards prescribe recording and reporting practices that are deemed to be acceptable when reporting on the financial affairs of an entity. (IFRS, 2012).

In South Africa (SA), the Accounting Standards Board (ASB), used to issue SA GAAP which was based on international standards, but SA GAAP was withdrawn in 2012. For financial years commencing on or after 1 December 2012, South African entities should use IFRSs (International Financial Reporting Standards), as approved by the IASB (South African Institute of Chartered Accountants (SAICA), 2012). Externally communicated information must be prepared in accordance with IFRSs to ensure the same understanding of the information by both the preparers and users of that information. The financial statements of schools in South Africa should therefore be consistent with the requirements of IFRS. The enforcement of accounting standards improves the quality of financial reporting.

The literature recognises that measuring the quality of financial reports like the financial statements is problematic especially because different users may perceive the usefulness of information very different from each other (Botosan, 2004; Daske and Gebhardt, 2006).

However, it is a fact that most of the stakeholders in schools will not have the ability or need to analyse the financial statements in detail or test the compliance with accounting standards. This study will therefore not test whether the sample financial statements adheres to all the requirements of IFRS but will rather concentrate on the quality in terms of fundamental characteristics like relevance and faithful representation which are enhanced by characteristics like understandability, comparability, verifiability and timeliness. This study therefore concentrates on the quality and therefore value of the financial statements of schools to discharge their financial accountability to the parents, sponsors and general community. Stakeholders in schools like the parents and community members are probably only interested in whether the statements are trustworthy, that no corruption took place, the budget were complied with and that the school is in a position to provide value for money. To enable this it is extremely important that the statements are transparent and easy to understand. Understanding the information contained in the financial statements is a key step to making informed decisions, especially

during budget adoption. Parents and other members of the community should also serve as “watchdogs” and possible areas that can reveal mismanagement or corruption should be identifiable and clear. As stakeholders become more involved in the management of schools and in holding governing bodies accountable as is the vision of the government, they will become more skilled in financial matters and the quality and clarity of the financial statements of South African schools will therefore probably become even more important.

The format, contents, and value of financial statements of schools are briefly explored in the next part.

Format and contents of financial statements

According to IAS1 *Presentation of financial statements*, paragraph 10, a complete set of financial statements comprise:

- a statement of financial position as at the end of the period (balance sheet);
- a statement of profit and loss and other comprehensive income for the period (income statement);
- a statement of changes in equity for the period;
- a statement of cash flows for the period; and
- notes, comprising a summary of significant accounting policies and other explanatory information. (IFRS, 2012: A562).

An auditor’s report will accompany the financial statements if these were audited.

Although each of the financial statements has its specific purpose, the statements are of equal importance and are interrelated (IFRS, 2012: A563).

Financial statements are usually presented on a comparative basis (for more than one year) to allow users to easily spot significant changes (IFRS, 2012:A569).

The value of financial statements of schools

Accounting theory has long recognised that financial reporting (as in financial statements) is based both on a decision-usefulness paradigm and a stewardship rationale (Coy, Fisher & Gordon, 2001:2). The New Basic Financial System for Schools (WCED, 2013:36) Western Cape Department of Education list the objectives of financial statements as follows:

- give effect to legislative requirements of the South African School’s Act as well as Section 38 of the Public Finance Management Act (PFMA), Act 1 of 1999 (Republic of South Africa, 1999);
- provide guidelines to the finance committee;
- indicate the financial position, financial performance and cash flows of the school;

- show the results of management's stewardship of the resources entrusted to them. The financial statements also
- form the basis for decision-making regarding financial matters;
- provide a means of tracking the growth or decline in a school's assets or liabilities;
- form the basis for determining the value of school property;
- provide a means for budgetary control, for instance by comparing actual financial results with legally adopted budgets; and
- provide data to target specific areas for improvement.

Different stakeholders or groups of stakeholders may use the financial statements for different reasons but they will all perform some form of analysis of its contents to interpret the information in the financial statements.

Financial statement analysis

Shim (2008:2) describes financial statement analysis as: 'a process which examines past and current financial data for the purpose of evaluating performance and estimating future risks and potential'. Koen & Oberholzer (2002:3-5) describe financial analysis as the measurement and evaluation of information in financial statements in order to make the information more useful for decision making. The results of the analysis are interpreted by seeking the reasons for, and the repercussions of the results for the entity. Analysis can be seen as the link between the financial statements and the decision-making process.

Steyn, Warren and Jonker (2004:11) stress the importance of comparing current financial statements to those of previous years or with similar enterprises. This will highlight areas which are different or have changed. Users can then establish the reason for the difference or change and see whether it is positive or negative. A stable historical track record is usually an indication of a financially sound school.

By comparing the financial statements with the budget, users are able to judge whether actual performance is in line with planned performance.

A user can also identify unexpected variances and trends that do not meet expectations. This may bring to light issues that need further attention.

Koen and Oberholzer (2002:11) suggest the following basic steps for analysis.

- Examine the auditor's report and director's report (principal's report in a school) for any exceptional comments.
- Study the accounting policy and notes to the financial statements.
- Examine the cash flow statement with special attention to the purchase and disposal of assets or possible restructuring of financial resources.

More in-depth analysis like financial ratios, etc. can then be applied to areas of concern.

Analysis specific to school financial statements

Public sector entities like schools are expected to be accountable for:

- the extent to which the entity performed in accordance to its financial plan;
- the extent to which current activities/results have an effect on the activities/results of future periods; and
- the financial condition of the entity

Schools do not have profit as their main purpose, but rather good education, and unlike profit-oriented businesses, a school's resource allocation is often set by policy rather than by forces of supply and demand. When looking at a school's financial statements, one should therefore first consider whether the school has complied with the relevant rules and regulations.

In South Africa, school financial statements have to comply with the following legislative prescripts and regulatory framework:

- GAAP (or IFRS from 1 December 2012)
- The South African Schools Act, Act 84 of 1996, Sections 43(1) & (2)
- The Public Finance Management Act, Act 1 of 1999
- Circulars issued by Education Departments (WCED, 2013).

Secondly users must consider the school's financial position and judge whether its financial performance was satisfactory.

Those things in the financial statements that relate to **financial position** are:

1. The assets and liabilities of the entity
2. Cash and cash equivalents
3. Debt and other liabilities
4. Other resources

The financial statements provide information regarding **financial performance** through:

5. Budget compliance
6. Annual surplus/deficit
7. The extent to which revenue of the current period is sufficient to cover the cost of providing services in the period plus any costs of previous years that were not covered by revenue in previous years
8. A change in net assets/liabilities
9. A change in net debt/net financial assets
10. The sources and uses of cash.

Other information which can be obtained from the financial statements are:

- Did the school receive enough cash to cover operations, or is it using its reserves?
- How much of the available funds are spent on teaching activities?
- How much money did the school raise from a specific fundraising project?

- Does the school have the ability to meet its obligations – will the school be able to pay its bills and repay any debts?
- Is the school better or worse off financially than the previous year and why?
- How much (cash, fixed assets, equipment, etc.) does the school own?
- How much money does the school owe?
- Are there any looming issues that may affect finances in the future?

The audit report is the final stage of an audit of annual financial statements.

Audit

The South African School's Act in section 43 requires that financial statements of schools are audited, and that an auditor's report should be submitted together with the financial statements.

According to both the International Standard on Auditing 200 (ISA200) and the South African Auditing Practice Statement 2 (SAAPS 2), the main objective of an audit of financial statements is to enhance the degree of confidence that users of financial statements place on the information presented in such statements. An audit involves performing procedures to obtain evidence about amounts and disclosures in the financial statements. An audit enables the auditor to form an opinion on the accuracy of the financial statements prepared by an entity (for instance a school) for a given period. (SAICA, 2012).

The audit opinion is intended to provide reasonable assurance that the financial statements are presented fairly, in all material respects, and/or give a true and fair view in accordance with the financial reporting framework (ISA700). The recognised financial reporting frameworks in South Africa are IFRS and GAAP. An audit should therefore confirm that the school has handled the financial records in accordance with GAAP/IFRS.

The secondary objective of auditing is to detect or prevent errors. By promoting transparency and accuracy in the financial disclosures made, auditing reduces the possibility of unscrupulous dealings being concealed. Auditing ensures that managers use accounting rules and conventions consistently over time and that any estimates are reasonable.

Financial audits are typically performed by firms of practicing accountants who are experts in financial reporting. The fact that the external audit is done by someone with special knowledge provides assurance that the financial statements are acceptable.

According to Hack, Candoli and Ray (1998:170), auditing is the final stage in the process of managing school funds and helps to improve the school's accounting system. Auditors' reports also help school governors to "build bridges of confidence" with stakeholders.

Appointed auditors do not examine every transaction, nor do they guarantee that the financial statements are completely accurate. Because of the test nature and other inherent limitations of the annual audit, together with the inherent limitations of any accounting and internal control system, there is unavoidable risk that some material misstatements may remain.

An audit report should be clear, constructive and concise. The auditor should point out in writing:

- any weaknesses/strengths in the accounting system of the school
- deficiencies in the financial control system
- inadequacies in the financial policies and practices
- non-compliance with accounting standards and legislation.

The report should also explain any implications of the above points and give advice or recommendations for improvement. The auditor should give in clear terms his/her professional opinion on the state of the accounts.

The auditor's opinion can be unqualified, qualified or adverse depending on the records and any other evidence the auditor may have examined and evaluated. An unqualified opinion is positive and satisfactory and a qualified opinion indicates that the auditor has some reservations about the state of the school's accounts (ISA 700(Revised), par 40-41).

In the light of the above, a discussion of the analysis of the financial statements of four ordinary South African schools follows in the next section.

Preliminary evaluation of four sets of financial statements of schools

Availability

Section 43(6) of the South African Schools Act states that "at the request of an interested person, the governing body must make the records referred to in section 42, and the audited or examined financial statements referred to in this section, available for inspection". A large number of schools in South Africa have websites where they provide extensive information about their particular school. These websites are used both as promotional platforms to encourage potential learners to enrol in the school as well as information platforms for current parents and learners. A school's financial state will probably influence the facilities available at the school, curricula choices offered by the school and the school fees payable. One would therefore assume that prospective scholars and parents will be interested in information in this regard. It would therefore seem logical that a school should provide some financial information on its website and seeing that financial statements are the main method of external financial communication, one would expect to find these statements on the websites although it is not an

official requirement. An attempt was therefore made to try and find school financial statements on the internet.

The SA Schools web site, listing 516 web sites of schools in South Africa was used as basis as on 8 August 2012 (SA Schools, 2012). A statistical sample of 25% (every fifth web site) was selected and 129 web sites were thus identified. In cases where web sites were inaccessible or did not exist anymore, the next available web site was visited. These web sites identified were visited searching for annual financial statements.

Only three sets of financial statements could be obtained in this manner. In other words, only 2,3% of the 129 schools provided their financial statements on their websites. As this was a rather extensive search, it can be concluded that schools very seldom publish their annual financial statements on the internet.

A number of schools in Pretoria were then phoned to obtain their financial statements but it soon became clear that schools, as represented by the school principals, were not willing to provide their financial statements despite section 43(6) of SASA. The reason indicated in most cases was that the statements are confidential.

One extra set of financial statements was obtained on the basis of personal contacts with a school, therefore a total of four sets of annual financial statements were available for this study.

The compliance of these financial statements regarding the requirements of the Schools Act and GAAP was then evaluated regarding the following predetermined areas of interest:

- Timeliness of the publication of the annual financial statements
- Comprehensiveness of the annual financial statements
- The audit report
- Bank account
- Non-current assets with specific reference to property, plant and equipment.

Timeliness of the publication of the annual financial statements

As indicated earlier, financial reports must be prepared on a timely basis to be effective. The Schools Act, section 42(b), also prescribes specific time frames in which the financial statements must be prepared and submitted. Audited annual financial statements must be prepared by each school within three months after the end of each financial year.

Three of the four sets of annual financial statements were published within the three months period as prescribed.

One set of annual financial statements for the year ended 31 December 2011 was only published on 12 April 2012, thus 12 days late. Even though this date falls outside the prescribed three-month period (31 March 2012) it still is a very reasonable period

after the required date and therefore does not seem to be a reason for concern.

Comprehensiveness of the annual financial statements

A complete set of financial statements comprises the following (IFRS, 2012:A562):

- A statement of financial position as at the end of the period.
All four schools complied.
- A statement of profit or loss and other comprehensive income for the period.
All four schools complied.
- A statement of changes in equity for the period.
All four schools complied.
- A statement of cash flows for the period.
Three schools complied. One school did not include a statement of cash flows but included a "statement of receipts and payments". Even though useful information was provided in this manner it is not in accordance with the IAS 1. A statement of cash flows should have been provided and the "statement of receipts and payments" should have been given as additional information if so required by the users of the financial statements. No further explanation was given in the statements, or elsewhere, as to the reason for this deviation.
- Notes, comprising a summary of significant accounting policies and other explanatory notes.
All four schools complied.

The audit report

Two sets of financial statements received an unqualified audit report. The other two had qualified opinions.

One audit report stated the following opinion qualifications:

"It was impractical for us to extend our examination beyond the receipts actually recorded"; and "the assets were not audited".

This is of concern taken into consideration that schools often have extensive assets at their disposal and control. It might indicate serious problems regarding the control of cash received and asset management but the extent of this could not be ascertained from the audit reports.

The other audit report did not mention assets at all, despite the fact that it was stated in the accounting policies that property, plant and equipment is written off in the year of purchase. This definitely raises the question of whether the financial statements provide a fair representation of the financial position of the school. Obviously, in this case assets were also not audited. It can be argued that by writing off all assets and then not referring to this at all in the audit report is an attempt by the auditors to absolve themselves from any responsibility regarding the assets of the school. This seems unacceptable.

Bank account

According to the South African Schools Act 84 of 1996, section 37(3) "The governing body of a public school must open and maintain a banking account."

All four schools have a bank account.

Non-current assets with specific reference to property, plant and equipment

According to the South African Schools Act 84 of 1996, section 37(5) "All assets acquired by a public school on or after the commencement of this Act are the property of the school." Section 42(a) also state that the governing body of a public school must "keep records of funds received and spent by the public school and of its assets, liabilities and financial transactions". The best way to "keep record of its assets" is to include all assets of the school in its financial statements and to present it as such to the users of a school's financial statements. Assets should also definitely be audited.

Of extreme concern is that only two schools actually had the line item "Property, plant and equipment" in the Statement of Financial Position with appropriate policies and notes. The other two schools wrote down (depreciated) all the assets to Rnil in the year of purchase as an expense! This is in direct contradiction to the above mentioned requirements of the SASA. This is also in direct contradiction of the International Accounting Standard 16, paragraph 1 (Property, Plant and Equipment). Paragraph 1 state: "The objective of this Standard is to prescribe the accounting treatment for property, plant and equipment so that users of the financial statements can discern information about an entity's investment in its property, plant and equipment and the changes in such investment. The principal issues in accounting for property, plant and equipment are the recognition of the asset, the determination of their carrying amounts and the depreciation charges and impairment losses to be recognised in relation to them".

To exacerbate the situation even further, is the fact that the two schools writing down these assets to Rnil, spent material amounts on assets. Large amounts were spent on items like vehicles, computer equipment and sport equipment that just 'disappeared' from the annual financial statements. This practice can definitely encourage both misuse and theft, and the "concealment" thereof should be addressed as a matter of urgency.

Conclusion

As this is an exploratory study with only four sets of annual financial statements examined, no conclusion can be made representing South African schools as a group. Section 95(1) of the Constitution of South

Africa (Republic of South Africa, 1996a), prescribes the fostering of transparency by providing the public with information. SASA also demands that financial statements should be available to interested parties. The fact that schools do not want to provide the financial statements therefore seems suspicious, especially because these statements contain the basic information that will indicate to parents and taxpayers where their money is going.

It is also clear from the above analysis that financial reporting by schools is not consistent. Schools also do not always comply with SASA, or with IFRS/GAAP, in preparing their annual financial statements.

Practices regarding the recording, reporting and auditing of assets indicate a real risk of potential corruption and concealment of misuse or even theft of assets. The variations found in the financial statements that we examined have the potential to influence decision makers who rely on the financial data provided.

It appears that schools in South Africa are held to different standards of financial reporting and auditing than commercial firms and therefore it can be questioned whether assets are properly protected.

The evidence from the literature regarding lack of feedback on the submitted financial statements by the education departments to schools combined with the clear indication that schools are not always compliant with statutory requirements and do not always adhere to proper accounting procedures, seem to indicate that schools are allowed to function outside legal requirements without consequence. This is of great concern.

It is therefore concluded that a more comprehensive and representative study of the contents of financial statements of South African schools is urgently needed to establish the extent of compliance or non-compliance with regulatory frameworks. Audit practices regarding the schools should also be investigated to ensure public trust.

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OPERATIONS AND QUALITY MANAGEMENT FOR PUBLIC SERVICE DELIVERY IMPROVEMENT

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Abstract

Public service management reforms have not yet contributed to poverty eradication and generally socio-economic development of many African countries. The reforms suggested and implemented to date still prove to be weak in addressing the many challenges faced by the public service in delivering goods and services to the population. The failure of the current public service management calls for a consideration of business-driven approaches and practices that facilitate effectiveness, efficiency, competitiveness and flexibility in goods and services provision. The critical social theory methodology and the literature review technique described and raised awareness on service delivery chaos in South Africa. A public service reform that focuses on operations and quality management is one of the ways of improving and sustaining service delivery in South Africa. Operations management is an essential tool for the planning, execution, control, monitoring and evaluation of production processes. Quality management, in the other hand, is essential to ensure best quality of goods and services produced by the public service within acceptable time and available resources to meet or exceed people's expectations. The operations and quality management framework proposed in this article is a potential alternative to the current service delivery crisis in South Africa.

Keywords: Operations Management, Quality Management, Service Delivery, Public Service, Governance

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1. Introduction

The delivery of public goods and services to the satisfaction of the people has been a dilemma of the South African democratic government. The ruling party's motto "better life for all" and the public service's "good governance for service delivery" approach portrayed as a ways of doing things right, seem to amount to just useless slogans as goods and services delivered do not address the public's needs resulting in protests some being violent.

It is certain that many governments don't function the way they should in order to deliver goods and services to the people for various reasons. Mc Lennan (2009) talks about a state-driven goods and services delivery system in South Africa whereby politics define a power relationship between the state, the citizens and the economy. This perspective supports the idea of Rogers (1978) about the limitations of public service to deliver goods and services because of expertise and political biases. Rogers (1978: 1) advocates the transfer or adaptation of management practices that work well in the private sector into the public service. He argues that the traditional way of managing public service was not successful and that using the business management

models could be a solution. He emphasised the need for the public service to be run like private companies thus the potential effectiveness of the management transfer approach (Rogers, 1978: xi).

Although Rogers's experience and suggestions for fixing the mismanagement of New York City is ancient and might not be similar to the current service delivery crisis in South Africa, some of his critical questions in the search for improving and sustaining the management of the public service remain of actuality. Rogers (1978: 1) asks two important questions of relevance to the current service delivery crisis in South Africa. Firstly, he questions whether the management practices and expertise of business can be transferred to the public service especially the local government. Secondly, he probes the types of business-based management practices and expertise that can be transferred to the public service and with what adaptations.

These two questions remain valid and inform the hypothesis that business management practices and expertise can facilitate goods and services delivery in the public service. These questions also prompt the selection of operations and quality management, two types of management techniques that prove to produce good outcomes in the business

sector and which, if modified and adapted to the public sector can facilitate public goods and services delivery.

Operations management is essential in maximising the production of goods and services in the public service whereas quality management assures the satisfaction of beneficiaries beyond their expectations. The basic principles of operations management and those of quality management are considered to facilitate goods and services delivery. To such end, the operations and quality management framework (O&QMF) proposed in this article describes how operations and quality management principles, practices, process and application can facilitate goods and services delivery in the public service.

The research leading to this article is the reflection of critical social theory aiming at understanding the way the society functions in order to introduce theories facilitating social change. A literature review facilitated data collection, analysis and interpretation. A modelling technique assisted the development of the in proposed O&QMF. The literature review consisted of recording how operations management and quality management can facilitate production. The review of good practices on operations management and quality management in the public service informed the development of the O&QMF. The O&QMF will assist government entities not only to maximise the delivery of goods and services so as to satisfy the needs of the public beyond expectations therefore being effective, efficient, competitive and flexible.

2. Literature Review

This section reviews the definitions of the operations management and quality management and assesses how operations and quality management facilitate production and customer satisfaction. Practical examples of the success of operations and quality management in the public service are also reviewed to inform the research and the envisaged framework.

2.1 Operations and quality management for production and customer satisfaction

Nowadays, business organisations strive to remain in the market and therefore the production of goods and/or services becomes a challenging exercise. The cost and time for the production and the quality of goods and/or services produced are therefore critical considering competitions in the business sector. Many strategies are therefore developed and implemented in order to survive the competition. Operations and quality management are among the strategies used by the survived business organisations. Operations management deals with processes for production whereas quality

management completes the production process by assuring customer satisfaction. In the one hand, the task of operations management is to plan, execute, monitor and evaluate the processes of the production of goods and/or services. In the other hand, quality management is about assuring good quality of products or services.

Barndt and Carvey (1982: 1) define operations management as the process of planning, organising and controlling operations to reach objectives with efficiency and effectiveness. They view operations as processes to transform resources in order to create a result in the form of a product or service. Operations management is the process of transforming inputs or resources into desired outputs/goals or products and/or services. Operations management has therefore two subjects: production management and service management. In public service these two subjects relate to the role and the mandate of government to provide goods and services to the people in order to better their lives.

For Tuomi (2012: 12), quality management is internationally recognised under the International Organisation for Standardisation (ISO) 9001. ISO 9001 specifies the requirements for a quality management system. To fulfil the standard, an organisation needs to demonstrate its ability to consistently provide a product that meets customer and applicable regulatory requirements and its ability to enhance customer satisfaction through the effective application of the system. All requirements of the standard are generic and intended to be applicable to all organisations, regardless of type, size and product provided. This means that quality management can be applied in the public service in order to inform specified standards for products and services that meet the needs of the customers like any other organisation.

Tuomi (2012) argues that quality management means applying a system in managing a process to achieve maximum customer satisfaction at the lowest overall cost while continuing to improve the process. Stebbing (1990: 19) considers quality management as managing all functions and activities necessary to determine and achieve quality. For the author, quality management is a management technique that facilitates competitiveness meaning providing a product or service to satisfy the needs of the customer. The public service, having to serve the population that has a multitude of needs, has to focus on the quality of its goods and services as they relate to improving people's living conditions.

2.2 Operations Management and Quality Management in the Public Service

Before suggesting the use of operations management and quality management in the South African public service to facilitate service delivery, it is cautious to review some success stories about their

effectiveness elsewhere. Pollitt & Bouckaert (2004: 13) cited by Tuomi (2012: 6) argue that public management refers firstly, to the activities of civil servants and politicians. Secondly, it refers to the structures and processes of executive government, meaning for instance, using a technique such as Total Quality Management (TQM) in providing public goods and services. Peters and Savoie (1998: 15) acknowledge that three main innovations have taken place in public service management since the 1980s of which strategic management or planning or operations management and quality management.

Scharitzer and Korunka (2000) cited by Stringham (2004: 187) argue that the adaptation of quality management in the public service is entirely consistent with government's move to make the administration more efficient, more powerful, sleeker, and more citizen-oriented. They suggest that quality management reflects the new public management approach in applying performance-oriented programs. The three case studies below illustrate how operations management and quality management achieved good results in the public service.

2.2.1 The Management by Project in New South Wales

The New South Wales Department of Public Works and Services embarked on a public service reform to improve service delivery through a Managing by Project (MbP) system. The MbP system provides a flexible structure that assists in responding rapidly to environmental changes and in particular to changes in government direction without undergoing a complete organisational restructure (Crawford, Simpson and Koll, 1999: 2-3).

The MbP applies operations management through project management skills and includes quality management in order to satisfy the needs of the users. Through MbP, work is divided into different projects executed by dedicated project team members. The MbP focusses on the results while being flexible to deal with changes and delivering goods and services through cross functional and cross disciplinary project teams (Crawford et al., 1999). The authors quote Beltrami (1992: 770) who distinguished quality to signify the respect of norms and procedures; effectiveness; and customer satisfaction.

The MbP approach ensures the clear definition and alignment of the objectives to the vision, mission and goal. MbP also enables the effective use of resources; and the use of planning, control, monitoring and evaluation systems (Crawford et al., 1999).

2.2.2 Quality Management in Malaysian Public Service

Quality management was institutionalised in the Malaysian public service in 1991 through the Prime Minister's Department. Three programmes were implemented: the Quality Control Circle (QCC), the Client Charter (CC) and the Total Quality Management (TQM). Asim (2001) argues that all three programmes did not function as smoothly as planned, but immense success was recorded in the management of public service using quality management principles. The lack of commitment by some staff members was one of the difficulties in the implementation of quality management in the Malaysian public service (Asim, 2001: 9). Positive aspects of quality management in the Malaysian public service include improvement of work procedures and methods, the economic use of resources and improved motivation of employees according to Sarji (1993: 110) cited by Asim (2001: 9).

2.2.3 E-government: a strategic operations management framework

Affisco and Soliman (2006) based on the World Bank's assertion that applying information and communication technologies (ICTs) in government agencies can better their management and increase service delivery, argue that e-government is a coherent strategy for public goods and service delivery. E-government is a strategic operations management technique to facilitate public goods and services provision according to the authors. E-government is one of the priorities of the public service reform in South Africa: to maximise the use of opportunities created by the accelerating access to the Internet and ICTs (Ayeni, 2002).

Affisco and Soliman (2006) refer to their model as the strategic operations management framework for e-government service delivery (EGSD). The model represents a response to the need for a more strategic point of view on the electronic delivery of government services (Affisco and Soliman, 2006: 16). The importance of e-government is that it facilitates service delivery and at the same time collects from and provides information to the consumers or service users. E-government can therefore be used as a quality assessment tool by the beneficiaries of public goods and services.

3 Research Theory and Methodology

The research leading to this article used critical social theory based on a qualitative method through a literature review technique. The modelling technique was used to develop the suggested O&QMF.

3.1 Critical Social Theory

Critical social theory is a good approach for public administration research. Box (2005:14) argues that public administration is an area of research that has uncertain boundaries. Researchers and scholars are therefore reluctant to call public administration a discipline because it lacks theories proper to itself according to the author. However, the author infers that critical theory offers critiques of public institutions and possibilities for a better future. This article is concerned about the way the South African public service has failed to deliver goods and services to the population. In looking for a better future, the research proposes a business-driven approach to facilitate, improve and sustain goods and services delivery.

Box (2005: 16) argues that “A primary characteristic of critical theory is the idea that social systems change over time because of built-in tensions, or contradictions, between how they are and how they could be”. The current violent service delivery protests in South Africa demonstrate that the service delivery system is flopping. Critical social theory is therefore a good approach to question what is happening and how to implement positive changes.

To be specific, critical social theory consisted of three processes in this research. Firstly, the research considered systemic contradictions within the service delivery status quo in South Africa. The current service delivery system does not work and needs to be modified. Secondly, the dialectic process assisted in acquiring new knowledge alternative to the status quo through argumentation. The research was more exploratory than hypothesis-based focusing on understanding service delivery chaos to suggest solutions for improvement and sustainability. The suggested O&QMF responds to the third process of the research, to use the new acquired knowledge to facilitate change. The framework will improve and sustain the delivery of goods and services to the population to or beyond expectations.

3.2 Qualitative Method

The research was qualitative and used the literature review technique. This research technique facilitated the understanding of the service delivery chaos in South Africa, the failure of the public service reform as well as the learning from the success of the implementation of operations management and quality management in the public service through the three cases studies reviewed.

3.3 Modelling

The O&QMF was developed to facilitate service delivery in the public service in South Africa. It is a business-driven management system based on operations management and quality management. The

development of the O&QMF is explained in the following section.

4 The Operations & Quality Management Framework

Implementing operations and quality management in the public service means redesign in order to respond to questions such as how to improve productivity, how to reduce response times, how to reduce the cost of production, how to improve quality in order to meet customers’ expectations. Bamford and Forrester (2010: 2) argue that the aim of any service, retail, industrial public service, is to deliver goods and services of the quality, quantity and availability that will satisfy the customers’ needs while at the same time making most effective use of resources. This assertion classifies quality management as an integral part of operations management. The O&QMF adopts Bamford and Forrester’s inclusion of quality management as part of operations management.

The O&QMF includes two plans: an operations plan and a quality plan to facilitate the planning, management, control, monitoring and evaluation of goods and services delivery by the public service. It is important to echo that introducing business-driven management approaches into the public service system is not an easy task. Firstly, operations management and quality management are management tools that were designed to be used in the manufacturing and service industry sectors. Stringham (2004: 185) questions the applicability of manufacturing techniques and approaches into the public service delivery. The author argues that such techniques should be modified and adapted to the realities of each public service entity concerned.

Frost-Kumpf (1994) cited by Stringham (2004: 185) believes that many authors who write about quality management and its potential for application in the public service too frequently describe a system that promises too much and ultimately delivers too little. The management of the business sector is driven by the maximisation of profit, the design of goods and services to satisfy the customer and to motivate employees. This must also be the ideal for public service entities. For Swiss (1992) cited by Stringham (2004: 186), quality management can have a useful role to play in government, but only if it is “substantially modified to fit the public service’s unique characteristics.” This author responds to the early warning signal of Rogers (1978) about the revision of business-driven management tools before their use in the public service.

To be a customer focused as suggested by Asim (2001), quality planning need to heavily depend on the Integrated Development Plans (IDPs) process in South Africa. The IDPs focusses on public participation for the service delivery system to satisfy the needs of the users beyond expectations. Quality

issues need to be part of the IDP process. Public goods and services must be people-driven and based on the available resources without compromising the quality.

The Operations and Quality Management Model (O&QMM) is the basis for the O&QMF. It adopts the operations management inclusive of quality management and project management as proposed by Bamford and Forrester (2010: 2). The model has three phases. The first phase is the design of operations processes, products and services as well as the planning of goods and services quality. The second phase is the implementation of project plans and at the same time the monitoring of quality issues. The third phase is to ensure that goods and services are delivered and that their quality is up to the set standards. This model responds to Barndt and Carvey (1982: 3) assertion that the purpose of any operations system is to add value over and above the costs of inputs and transformation processes. They further argue that when the input-output system produces a negative value added in government operations, public support is withdrawn. This is when service provision protests and indignation start in South Africa.

4.1 The Principles of the O&QMM

The O&QMM is based on five principles or key performance indicators (KPIs) by Bamford and Forrester (2010: 3-4). They are quality (specifications to satisfy the customer: getting things right); speed (how quick products and services are produced and delivered: doing things quickly), dependability (reliability to customer: doing things consistently and on time); flexibility (ability to adapt and respond to different needs: being able to change); and costs (expenses to produce and deliver products and services: doing things cheaply). These KPIs can easily be implemented within the public service. The authors suggest that in an ideal world, operations management should facilitate the optimisation of these five KPIs.

Operations management is important in designing the structure and techniques of the business process. These techniques must then convert the inputs (materials, labour, information, processes,...) into outputs (goods and services) through the planning, implementation plan or projects and control, monitoring and evaluation framework based on the mission, vision, values and objectives of the public service entity.

The conceptual model of operations management by Bamford and Forrester (2010: 25) includes among other things: designing products and services (including quality planning); controlling the resources; managing projects; managing operations strategically; managing quality systems and improving the operations. This model seems too complicated for a government entity because of the

sophistication and the need for high expertise. The O&QMM borrows from Bamford and Forrester (2010) as well as the general quality management (ISO 9001) principles. The scope and principles as well as the templates of the O&QMF for public service are explained below.

4.2 The Scope of the O&QMM

This article cautiously suggests the inclusion of quality management within the operations management system to respond to the two initial questions by Rogers (1978). The first question was: "can the management practices and expertise of business be transferred to public service (local government)? The second question was: "what type of management practices and expertise can be transferred, with what adaptations?"

The scope of the O&QMM is therefore an adaptation of operations management model by Bamford and Forrester (2010) plus the Managing by Project experience by Crawford et al. (1999). The O&QMM relates to the functions of the public service in designing, planning, controlling and monitoring and evaluating resources for the production and delivery of goods and services to satisfy the users.

To be different from a business oriented operations management, the O&QMM has three scopes, the operations and quality planning, project management and control and monitoring and evaluation. Each public service entity must have an operations manager responsible for the design, planning, execution and control (including monitoring and evaluation) of the goods and services delivered. The operations manager will be assisted by different project managers for various functions of the entity. Operations and quality issues should then be discussed in a structure comprised of the operations manager and all project managers. Quality management and control can therefore form part of a special project.

4.3 Principles of the O&QMF

Swiss (1992) cited by Stringham (2004: 184) believes that quality management can have a useful role to play in government, but only if it is substantially modified to fit the public service's unique characteristics.

The eight principles of quality management by ISO (2012) are therefore important to be considered when introducing quality management in the public service. A quality management principle therefore is an essential imperative or reference to operate and manage an organisation in order to improve performance so as to satisfy customers and achieve the objectives of such organisation.

The first principle is that the organisation needs to be customer-focussed. Because the organisation depends on its customers, it must understand and satisfy their current and future needs. The organisation must strive to meet and if possible exceed the expectations of its customers. Leadership is the second principle of quality management. The direction and unity of purpose of the organisation needs to be established by its leadership. To achieve its objectives each organisation must create an environment propitious for the full involvement of all its members. The mission, vision, values and objectives of the organisation must be understood and practiced by all its members. That is the third principle. The leadership must ensure full involvement of people at all levels of the organisation in order to maximise its performance.

The fourth principle is the process approach. This principle is more addressed by the operations management part of the O&QMM. According to the ISO (2012), a desired result is achieved more effectively and efficiently when related resources and activities are managed as a process. This principle prescribes the definition of a clear process to achieve the desired results, the planning of activities and the identification and measurement of the inputs and outputs of the process. The fifth principle is system approach management addressed by the project management component of the O&QMM. For ISO (2012), identifying, understanding and managing a system of interrelated processes for a given objective improves the organisation's effectiveness and efficiency. The control, monitoring and evaluation of activities in the O&QMM will facilitate the implementation of the operations plans through projects. The sixth principle is continual improvement which is considered to be a permanent objective of the organisation according to ISO (2012). After monitoring and evaluation, improvements must be recorded and plans for future improvement developed.

The seventh principle is factual approach to decision making meaning that effective decisions must be based on the analysis of data and information. Amongst other recommendation of ISO (2012), any decisions and action taken should be based on the results of logical analysis balanced with experience. The last principle is mutually beneficial supplier relationships. For ISO (2012), an organisation and its suppliers are interdependent, and a mutually beneficial relationship enhances the ability of both to create value."

Considering these principles, two major indicators need to be considered to assess the appropriate implementation and successful intervention of operations management and quality management in public service. Firstly, the adherence to the eight principles of quality management is very important. Secondly, the ISO 9001 must be verified

to justify the best quality of the goods and services provided.

4.4 Catalysts of O&QMF

Padovani and Young (2012) believe that local governments face similar problems in the provision of goods and services globally. The most crucial problems of concern which apply to this article are the absence of a profit measure; difficulty to measure performance; political and external influence in decision making; and insufficient resources. These problems can be resolved through what the OECD (1995: 7) refers to as catalysts for change. The OECD's and other catalysts are applicable in using operations and quality management in the South African public service as explained below.

4.4.1 Efficiency and cost-effectiveness

Crawford et al. (1999) argue that the growth of the public service throughout the world after the Second World War engendered significant pressures for change during the early 1970's. In Africa, the call for change in the management of the public service was introduced by the World Bank and the International Monetary Fund (IMF) in the early 1980's through the famous Structural Adjustment Programme (SAP). These two major lending banks believed that amongst other measures, the reform of the African public services would promote their effectiveness and efficiency in service delivery to maximise growth and development. De Montricher (1998: 109) cited by Crawford et al. (1999) believes that the primary focus of SAP was to reduce expenditures and improve government operations at the same time.

This catalyst implies the need for increased efficiency and cost-effectiveness to control and reduce public spending. This catalyst emphasises the application of operations management in the business of public service entities. Through operations management public service entities must accentuate strategic planning, management and control of the service delivery system (Peters and Savoie, 1998).

4.4.2 Competitiveness

The second catalyst for change is to attain a reduction in national differences in public services and increasing desire to enhance competitiveness of national economies as a result of globalisation according to OECD (1995: 7). Improving the quality of services to meet and exceed the expectations from individuals and business and responding to flexibly and strategic external change within the public services are then possible through the implementation of both operations and quality management.

4.4.3 E-governance or use of technology

The third OECD (1995: 7) catalyst for change in the public service is to use the opportunities offered by ICTs. McNabb (2009) believes that public service reform should consider not only a business-driven approach but it must also focus on a next-generation ICTs system that facilitates goods and services delivery. ICTs are vehicles that facilitate service delivery; they reduce time, distance and resources in the production and provision of services. An operations and quality management system that is based on and facilitated by an accessible ICTs platform is more likely to provide timeous and up to standard services.

4.4.4 Project Management Skills

Facilitating operations and quality management through projects is essential. The Management by Project suggested by Crawford et al. (1999: 3) justifies the role of project management in facilitating service delivery. The authors describe MbP system as the way to organise people and other resources to deliver products and services to satisfy our client's needs. MbP gives the best available people the best available resources through teamwork, leadership and project management principles to produce the best outcome for the clients. MbP breaks down artificial barriers between functions and business units by focussing on results not get bogged down in internal processes.

4.5 The Operations and Quality Management Model

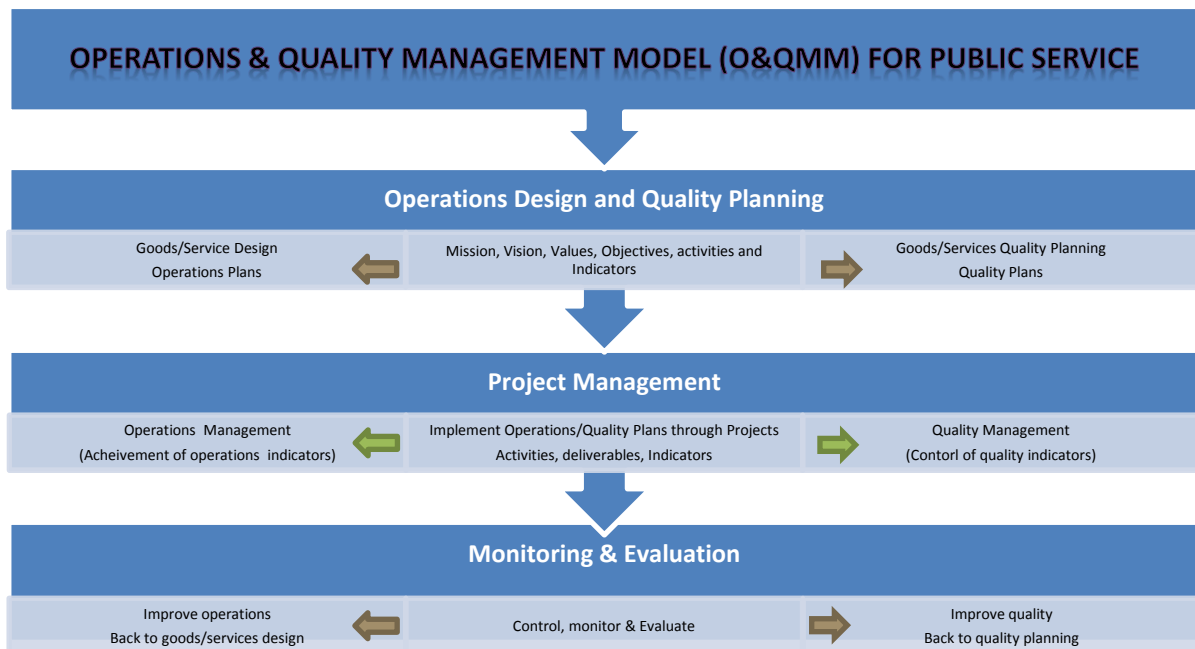
The O&QMM relies on the role to be played by the Operations manager. The operations manager, assisted by the project manager should develop the operations plans considering the mission, vision, values and objectives of the public service. Quality management issues must also be planed and contain in separate quality plans.

The project team is responsible for the implementation of the operation plans and quality plans. Each project manager should therefore be responsible for the indicators for each activity as well as the quality of the goods and services provided by the project. In this setup, there is no need of multiplying structures to have a separate quality officer. All project managers should therefore have a decision power and undergo project management and quality management training. They will also be in charge of the control, monitoring and evaluation of the activities as well as issues relating to quality. The overall control, monitoring and evaluation of all projects will be the responsibility of the operations manager as well as an external auditing.

In the public service an operations manager should have the rank of a director or chief director and the project manager should have the rank of director or senior manager. This will allow a good structure to include deputy and assistant directors as well as administrative and technical staff in each project.

The O&QMM for the public service is represented in the figure below:

Figure 1. Operations and Quality Management Model for public service



4.6 The Operations and Quality Management Framework

delivery. The O&QMF derives from the O&QMM above.

The template below shows the practical way of planning, implementing, controlling and monitoring and evaluating the process of goods and service

4.6.1 Template of the O&QMF

Table 1. Template of the operations and quality management framework

O&QMF Template					
	Operations			Quality	
Operations Design	Mission	Vision	Objectives		Quality planning
		Values			
Operations Management	Objective	Project	Operations Indicator	Quality Indicator	Responsible
Control Monitoring Evaluation					

Example of a completed O&QMF

Table 2. Completed O&QMF

O&QMF for the Gauteng Department of Social Development (2004 – 2009)					
	Operations			Quality	
Operations Design This design is led by Operations manager. Project managers participate. All projects are also discussed during this phase.	Mission	Vision/Values	Objectives		Quality planning
	To integrate and socially protect poor and vulnerable individuals, families and Communities of Gauteng.	Vision A society where poor, vulnerable and excluded individuals, families and communities are developed for an improved quality of life. Values “Batho Pele”			
			Contribute to the national effort to:		Description of key quality patterns for services:
			1. Fight poverty and build safe, secure and sustainable communities 2. Develop healthy, skilled and productive people		- Tangibility? - Reliability - Responsiveness - Empathy - Assurance ISO 9001 compliance for goods delivered

Operations Management	Objective	Project	Operations Indicator	Quality Indicator	Responsible
Project manager responsible for own project implementation and quality control.	Fight poverty and build safe, secure and sustainable communities	Grant delivery	All >18 years get the grant	Grant of + 500 per month	Mr Amisi Musa
		Provide housing to the elderly	1000 house delivered	House with 3 bedroom and equipped	Mrs Bawinile Ndlovu
	Develop healthy, skilled and productive people	Skills training for youth	600 youth are trained monthly	75% of trainees pass with + 65%	Mr Johan Viljoen
		Small business for unemployed	1000 people attend course receive grants	business growth by 10% in 6 months	Ms Vumilia Tabu
Control, monitoring and evaluation to be done per project activity					
Control	Objective clear? Yes	Project clear? Yes	1000 people trained? Yes	Business grew? Yes	Ops Manager
Monitoring	Objective linked to projects	Objective turned into Project	Indicator reached?	Service meets quality criteria?	Project Manager
Evaluation	Objective realised via activities?	Project reached objective?	All indicators achieved	Goods/services delivered up to quality?	External Audit

5 Conclusion

The initial questions of this research were to establish if the management practices and expertise of business could be transferred to the public service and to know what type of management practices and expertise could be transferred and with what adaptations.

Löffler (2001: 6) responds to these questions that quality has always played a role in the public administration. The author quotes Beltrami (1992: 770) who distinguished quality to imply the respect of norms and procedures; effectiveness; and customer satisfaction. The author argues that the meaning of quality in the public service changed in the late 1960s when management by objectives gained popularity in public administration. The management by project adopted in this article supports Löffler's argument.

The O&QMF proves the possibility of implementing operations and quality management in the public service to facilitate, improve and sustain service delivery. The O&QMF is a tool that combines operations management through management by project and quality management. The O&QMF observes operations management process of transforming inputs into outputs as well as the eight principles of quality management. The managing by project approach facilitates proper planning of operations and qualities of goods and services and considers strong control, monitoring and evaluation of the activities implemented.

The assessment of the quality of public goods and services provided by the public service through the O&QMF is necessary. Such assessment

constitutes a good question for further research. Parasuraman et al., (1988) as cited by Moura and Sintra ([Sa]: 19) proposes five dimensions in assessing service quality. They are, tangibility or the appearance of physical facilities, equipment, personnel, and communication material; reliability or the ability to perform the promised service dependably and accurately; responsiveness meaning the willingness to help customers and provide prompt service; empathy meaning the caring, individualised attention provided to the customer; and assurance or the knowledge and courtesy of employees and their ability to convey trust and confidence. Assessing the importance of the O&QMF in addressing the five dimensions above is therefore a good completion of this research in confirming the importance of business-based techniques in facilitating, improving and sustaining service delivery in the South African public service.

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A BAYOU PRIVATEER CRITIQUE'S MARCOUX'S FIDUCIARY ARGUMENT AGAINST STAKEHOLDER THEORY

*Emir Phillips **

Abstract

This Article critique's Alexei Marcoux's A Fiduciary Argument Against Stakeholder Theory which set the mark for Shareholder Theory. Stakeholder Theorists sense the denouement of Shareholder Theory, but perhaps this in-depth reassessment of Marcoux's Article may have them reconsidering. Recent corporate scandals reveal only the moral paucity of that company's management and are not conclusive evidence of any odious qualities inherent to either shareholders or Shareholder Theory. The theory that can throw out the bathwater and keep the baby will win. This article adheres to a modified Shareholder Theory elucidated therein while admitting that the human, all-too human Shareholder Theory evinces every fiber of our moral being when injustice harms that which we most love. This Article hopefully makes clear that Stakeholder Theory is best attainable within the legal rubric of 3rd party beneficiary analysis, which is a valid extension of Shareholder Theory. One can see the power of this when applied to a 3rd party beneficiary (stakeholder), thereby generally negating any further philosophizing as to a Stakeholder Theory when the legal contract principle of 3rd party beneficiary so readily inculcates it. Thus, Stakeholder Theorists can sleep at night, 3rd party beneficiary Contract Law is operating 24/7. The contracting 1st parties need only address important contingencies likely enough to warrant the transaction costs of express provision, such as the possible subsequent inclusion of 3rd party beneficiaries. For all other contingencies, the fiduciary obligation fills the gap. And so, while presently in an awkward position, Shareholder Theory has the advantage of being right, even if it desperately needed this Article to save itself.**

Key Words: Shareholder Theory, Stakeholder Theory, Shareholder Model, Stakeholder Model. Alexei Marcoux, Fiduciary, Exclusive Benefit Rule, Duty of Loyalty, Duty of Care, Pirate Jean Lafitte, BP, New Orleans

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I. Non-Fiduciary Stakeholder Theory

In I. Non-Fiduciary Stakeholder Theory, Marcoux delineates the two citadels of normative theories for corporate social responsibility, that of shareholder³ and stakeholder which have been determining what a corporation's role ought to be. Ethically speaking, corporate executives and managers should make

decisions according to the correct theory. Unfortunately, the two management theories are at loggerheads as to which is "right." This is no small matter since this combination of shareholder/management interests' bellies nearly every economy around the world and this analytical framework founds domestic and global institutions struggling to pull mankind out of the Hobbesian Reality that is.

³ Sometimes called "stockholder" theory, "shareholder" is used for consistency.

For Marcoux shareholder theory holds that managers are fiduciaries for and ought to manage firms in the interests of shareholders. The why of it is that shareholders advance capital to their managers, who then spend corporate funds in pursuit of...short-term⁴...long-term profit?...maximum value?...maximum dividend (infinite?) stream? The Father of this position is the almighty Milton Friedman who spoke, "There is one and only one social responsibility of business... to use its resources and engage in activities designed to increase its profits so long as it engages in open and free competition, without deception, *arriere-pensee* or fraud."⁵ Subsequently, Milton Friedman pronounced to management that their fundamental obligation is render to shareholders their just due: profits. It would be unethical to invest corporate funds in endeavors management found socially beneficial but that reduced shareholders' returns.⁶ Frankly, with these profits, shareholders themselves can give whatever amount to whatever charity they desire. The varietal skill of management is not needed, or sought after, to give the gift of money away.

According to Marcoux, stakeholder theory holds that management⁷ must orchestrate the equally valued interests of various stakeholders: usually shareholders, employees, customers, suppliers, and the community-at-large.⁸ Stakeholder theory⁹ justifies itself since managers have a (Kantian) duty to both the corporation's shareholders and "individuals and constituencies that augment a company's wealth-creating capacity and activities, and who are therefore its potential beneficiaries and/or risk bearers."¹⁰ The

most relevant distinction is stakeholder theory's demand that all stakeholders be duly considered even if it reduces company profitability.¹¹ The ultimate danger for Marcoux in implementing stakeholder theory is its insidious, inevitable and inherent terminus: that of eliminating management's fiduciary duty to their shareholders in exchange for an impossibly complicated weighing and balancing of stakeholder interests, each vying for the supremacy of being the "equal" interest acted upon by management. Thus, an inevitable immoral danger awaits each and every stakeholder theorists by, sooner or later, terminating the fiduciary status of the very group most deserving of said status: the impoverished shareholders. For Marcoux then, at minimum stakeholder theorists are inevitably dangerous to all, and at worse, straight up: tenured ne'er-do-wells.

For Marcoux, non-shareholders can legitimately be viewed as (exclusive) "means" to the "ends" of profitability; whereas, under the (Kantian) stakeholder theory, the vital interests of multiple non-shareholders are also perceived as "ends."¹² Marcoux holds that, it seems, under no circumstance, can stakeholders have or acquire fiduciary duties. Any form of self-dealing or engaging in decision-making to further stakeholder interests is a clear breach of duty of undivided loyalty¹³, which is foundational to fiduciary duty. Any form of self-dealing or engaging in decision-making to further stakeholder interests is a clear breach of duty of undivided loyalty, which along with the duty of care is en toto the fiduciary duty and is wholly derived from Trust Law which is itself founded from private trust situation wherein the settlor's welfare is maximized if the beneficiaries captured all the benefits flowing from the trust. That is why the duty of loyalty required the trustee (herein corporate management) to act in the exclusive interest of the beneficiaries (shareholders). The exclusive benefit rule truncates any transaction or managerial

4 Mitchell, L. E. (2008). *The speculation economy: How finance triumphed over industry*. Berrett-Koehler Publishers.

5 Friedman, M. (1973). The social responsibility of business is to increase its profits. *New York*.

6 Ibid.

7 Throughout, the terms directors, executives and managers are generally used interchangeably. Strictly speaking, directors are members of the corporation's board and can be either executives or non-executives directors depending on whether they are responsible for day-to-day operations; whereas, managers run the business, but not necessarily as members of the board. This separation of management from ownership is achieved by this creation of the board of directors who manage the capital of the corporation subject to limitations on its activities set out in its charter or memorandum of association. Shareholders have only very limited rights over the capital in the corporation, in particular over its withdrawal from the corporation, usually in the form of dividends.

8 Marcoux, A. M. (2003). A fiduciary argument against stakeholder theory. *Business Ethics Quarterly*, 1-24. This 'pluralist' approach views the firm as a bundle of human assets and relationships of which corporate officials are agents of all stakeholders, *i.e.* shareholders, creditors, employees, customers, consumers etc... Penrose, E. T. (1995). The theory of the growth of the firm, 1959. *Cambridge, MA*. Hill, C. W., & Jones, T. M. (1992). Stakeholder-agency theory. *Journal of management studies*, 29(2), 131-154.

9 Only the normative version of the theory is being considered: how managers ought to behave. Certain versions of the stakeholder theory describe management's actual behavior; whereas, instrumental versions predict outcomes if management acts a certain way. Jones, T. M., & Wicks, A. C. (1999). Convergent stakeholder theory. *Academy of management review*, 24(2), 206-221.

10 Post, J. E., Preston, L. E., & Sachs, S. (2002). Managing the extended enterprise: The new stakeholder view. *California management review*, 45(1).

11 Stakeholder theorists have provided algorithms to mediate stakeholders' interests. Ellsworth, R. R. (2002). *Leading with purpose: The new corporate realities*. Stanford University Press. But in agreement with Marcoux, this Author does not see algorithmic formulae being utilized by management any time soon, if ever. So the point remains.

12 Hasnas views the "social contract" theory as providing a third normative paradigm equivalent to both shareholder and stakeholder theories. Hasnas, J. (1998). The normative theories of business ethics: a guide for the perplexed. *Business Ethics Quarterly*, 19-42. However, Donaldson, T., & Dunfee, T. W. (1999). *Ties that bind: A social contracts approach to business ethics*. Harvard Business Press. Chapter 9) seems to view the "social contracts" perspective as a meta-theory to help sort through the stakeholder obligations.

13 Essentially, Stakeholder Theory would require directors to be granted greater independence than they have at present wherein their sole legal duty is to the Shareholders, but this linchpin of Stakeholder Theory raises massive agency concerns about self-interested directors pursuing personal gain at the expense of the corporation. This Article would rather amend Shareholder Theory to inculcate into the corporate body more committed Shareholders (Owners) with less control put in the hands of Piratical Day-Traders only out for immediate Stock Price Treasure, these short-term shareholders and their kind must be endured but only as disempowering shareholders with little to no effect via the vote on management. So there are good privateering pirates, and not-so-good treasure-only Pirates.

mode of conduct that might also benefit management or one stakeholder (customer vs. employees) over another. It is specifically this adamant position by Marcoux that offends so many; and perhaps, rightfully so. But beware, Marcoux is duly enshrouded by Trust Law which he ironically (hypocritically?) uses to gut Stakeholder Theory and bolster the Contractarian viewpoint that is Shareholder Theory. Simply put folks, it's Trust Law vs. Contract Law.

B. Fiduciary Relations

Marcoux delineates the essential nature of a fiduciary relation by citing "Fiduciary," in *Black's Law Dictionary*, 5th ed. (St. Paul, Minn.: West, 1979), 563, which ventures back to Roman times to derive the original meaning of fiduciary's as a Trustee full of scrupulous good faith and candor. However, unfortunately for Marcoux, while the essence of fiduciary remained relatively static until the Industrial Revolution, since then and particularly in a corporate environment, Courts have viewed fiduciary as having more and more a contractual basis as opposed to Trust basis. This is somewhat farcical given that Marcoux wants us to end up with a Contractual viewpoint of shareholder/management relations.

Predictably, Marcoux then focuses on the 1st component of fiduciary: the Duty of Loyalty, rather than the Duty of Care. But like Janus, Fiduciary is bi-facial, one mien the duty of loyalty, the other duty: to really care, which conveniently enough, Marcoux fails to mention. To make matters worse, Marcoux's examples of fiduciary (doctor, attorney, and guardian) all involve non-C-corporate environments and are therefore by definition, non-shareholder examples, making their applicability to shareholder theory arduous at best. At worse, wholly irrelevant.

Fact is, the law tends to impose a fiduciary obligation whenever there exists an agency problem. Agency problems arise whenever one person, the principal, engages another person, the agent, to act in the best interests of the principal rather than his own.¹⁴ The gnawing fear is that when the agent's interests diverge from those of the principal, guess who loses (money). Agency problems are ubiquitous since who has the time, energy and skills necessary to do everything for themselves. The law steps in to fix this dilemma by imposing a fiduciary duty. In a corporate environment this is what transpires. Shareholders trust management and agree (contract) with management to act on their behalf in exchange for various forms of compensation. This duty of loyalty means corporate management should act appropriately when conflicts of interest exist.¹⁵

Under the exclusive benefit rule, this means 100% of management's efforts must work towards only shareholder interests. For Marcoux and Trust Law, to do otherwise is to violate one's fiduciary duty, which both involves legally culpable as well as unethical managerial behavior. Thus, stakeholder theorists presently advocate an impractical, unethical and illegal theory, making all proselytes to their cause nefarious accomplices. Why these public miscreants have been allowed to run amuck through business ethical journals is a query of queries.

Sadly, Marcoux makes this Section of his Article largely or wholly inapplicable by using inapplicable analogies, that of the professional class (doctor and attorney) as well as fiduciary duty based on status (Legal Guardian), neither of which readily applies to that of public (or closely held) corporate governance.

C. Stakeholder Theory and Fiduciary Relations

Multi-fiduciary stakeholder theory insists managers are fiduciaries for all the firm's stakeholders. But Marcoux notes that managers cannot simultaneously be fiduciaries for all of these groups since it is conceptually impossible to justly effectuate balance between the various and equal interests of the multiple stakeholders. Too many Chefs in the kitchen, firm failure is nigh guaranteed. Kant notwithstanding, no human or god can implement the interests of each of these groups simultaneously. Someone is going to get less than. The only question is who not if, particularly when each interest has an equal Kantian-nominal-Platonic weight at all times.

With the grist of multi-fiduciary theory apparently emanating from Immanuel Kant, it would follow that all stakeholder interests carry the transcendental weight of a Categorical Imperative and so the multitudinous process to fairly determine which interest should guide management decisions would be akin to driving a caravan of camels through the eye of a needle. Marcoux concurs with Hasnas who notes, it is unethical to take on fiduciary obligations to parties with conflicting interests in the same asset or project because there will come a time when it will be impossible to act as a fiduciary for all of them. In addition, according to Marcoux, on this point most stakeholder theorists and specifically authors Evan and Freeman would also concur. Little did these three souls realize this hyper-critical admission would cast their Beloved Stakeholder Model into the Inferno? But can they *cherchez la femme* Beatrice di Folco Portinari. As yet, Stakeholder Theorists have not articulated a viable methodology to resolve this inveterate thorn in the flesh. And until such time, 'tis no thorn, but rather, a driven stake betwixt the heart. Businesses must move

14 Jensen, M. C., & Meckling, W. H. (1976). Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of financial economics*, 3(4), 305-360.

15 Lorsch, J., & Young, J. (1990). Pawns or potentates: The reality of America's corporate boards. *The Executive*, 4(4), 85-87.

well in a tumultuous environment. A good ship has a Capitaine, not a concerned committee.¹⁶

II Morally Substantial Fiduciary Relations

Marcoux admits that for certain relationships (doctor-patient, attorney-client, guardian-ward) it would be morally wrong for these specific relations not to be fiduciary in character. But Marcoux misses the point entirely. These non-shareholder relationships never ever enter the realm of corporate governance. They simply do not apply and are entirely irrelevant since they involved non-shareholder, non-C-corporate realities and their fiduciary duty is primarily derived from Trust Law and not Contract Law from which corporate governance is headed towards more and more.

Stakeholders never seem to fully and truly acknowledge that the corporate fiduciary schemata bring to business not just skills *creme de la creme* but also deep pockets. Originally, trust law did not allow compensating trustees since any gentleman serving as a family stakeholder required no pay. This reality is long gone. Soon enough, legislation overcame the presumption against trustee compensation.¹⁷ Particularly within the realm of corporate governance, a contractarian view of fiduciary duty has become the dominant doctrinal current in modern American law. From corporations¹⁸ and partnership,¹⁹ to the law of marriage²⁰ to landlord and tenant,²¹ scholars increasingly perceive imputed bargains if they can be readily modified by actual bargains. Today, statutes empower trustees (management) to conduct every conceivable transaction to enhance the value of trust (shareholder) assets or wrest market advantage.

Fiduciary duties and remedies emerge from a single solitary common source: equity. This is why fiduciaries must account for ill-gotten profits even if their shareholders suffered no injury, which is a remedy in equity. Marcoux should not have muddied his position by conceding there are times when certain fiduciary relationships or duties apply, not to mention his analogies were all non-corporate and off

point given the ever-increasing contractarian basis for fiduciary relationships, particularly in the shareholder realm of C-corporate governance where the paradigm is *nigh Lord and King*.

Quite apropos is Roscoe Pound's *bon mot*: "Wealth, in a commercial age, is made up largely of promises." Modern wealth takes the form of financial assets. For example, insurance and annuity contracts, stocks, bonds, mutual fund shares, pension plans, and capital. The modern trust normally contains a portfolio of these complex financial assets, which are nothing but contract rights against the issuers. By comparison with a trust involving ancestral land, the modern trust fund affords greater resilience to accumulate, issue, or consume trust funds on behalf of 1st Party (Shareholder) and 3rd Party (Stakeholder) beneficiaries. Stakeholder theory too often crimps this wealth creating process.

The change of realty trust assets to that of financial assets, also transformed the identity of trusteeship from stakeholder (Trust Law) to management (Contract Law). Private trustees are still prevalent, but the quintessential modern trustee is corporate management, whose business is to enter into and carry out shareholder agreements. Marcoux fails to note that in the eyes of the law, C-corporations, as opposed to pass-thru entities such as an S-Corp. or LLC (not to mention Sole Proprietor) are for all intents and purposes: legal persons entitled to Due Process and at times, a fiduciary duty. After all, it was during Reconstruction, in the consolidation of Capitalism (via the Railroad) following the Yankee victory in the War of Northern Aggression, that Corporations were granted personhood. Anyone having a serious problem with this should have joined the Army of Northern Virginia. This, Marcoux seems wholly unaware of.²²

Simply put, shareholders in the aggregate make up a legal person (the corporation)²³, who enters into

16 The notable John Hasnas would agree with Marcoux on this point. Hasnas, J. (1998). The normative theories of business ethics: a guide for the perplexed. *Business Ethics Quarterly*, 19-42.

17 Langbein, J. H. (1995). Contractarian Basis of the Law of Trusts, *The. Yale Lj*, 105, 625.

18 Easterbrook, F. H., & Fischel, D. R. (1993). Contract and fiduciary duty. *JL & Econ.*, 36, 425; Butler, H. N., & Ribstein, L. E. (1990). Opting Out of Fiduciary Duties: A Response to the Anti-Contractarians. *Wash. L. Rev.*, 65, 1.

19 Recent revisions to the Uniform Partnership Act substantially augment the sphere for contract to defeat the default regime. Revised Uniform Partnership Act §§ 103, 404, 6 U.L.A. 288, 313 (1994).

20 The Uniform Marriage and Divorce Act encapsulate the modern position. Section 201 defines marriage as "a personal relationship... arising out of a civil contract." Uniform Marriage & Divorce Act § 201, 9A U.L.A. 160 (1973).

21 Glendon, M. A. (1981). Transformation of American Landlord-Tenant Law, *The BCL Rev.*, 23, 503; Chase, E. (1981). Property-Contract Theme in Landlord and Tenant Law: A Critical Commentary on Schoshinski's American Law of Landlord and Tenant, *The. Rutgers Lj*, 13, 189.

22 In *Santa Clara County v. Southern Pacific Railroad*, 118 U.S. 394 (1886), Chief Justice began oral argument by stating, "The court does not wish to hear argument on the question whether the provision in the Fourteenth Amendment to the Constitution, which forbids a State to deny to any person within its jurisdiction the equal protection of the laws, applies to these corporations. We are all of the opinion that it does." 118 U.S. 394 (1886) Two years later, in *Pembina Consolidated Silver Mining Co. v. Pennsylvania*- 125 U.S. 181 (1888), the Court clearly affirmed the doctrine, holding, "Under the designation of 'person' there is no doubt that a private corporation is included [in the Fourteenth Amendment]." The Court has since then reaffirmed this doctrine many times, even recently in *Citizens United v. Federal Election Commission*, No. 08-205 (1/21/10): corporations have the same political speech rights as individuals under the 1st Amendment. And even the Brits are in on it, *Jameel and Others (Respondents) v. Wall Street Journal Europe Sprl (Appellants)*, UKHL, 44 wherein the House of Lords upheld the corporate right to sue in defamation for reputational damage despite any specific evidence of pecuniary loss.

23 From this Promethean adventure, we have conjured up something that is both of ourselves and distinct from us. This something has morphed into a creature with characteristics not part of its creator's design. A faithful servant no more, our son, Frankenstein, must be captured and re-electrified to better suit the world he was created to tend. As an aside, all monsters are not in ratio, unlike Aphrodite. This entire macabre is the proper structural alignment, and not negation, of valid interests, the result

binding shareholder agreements with management. Yet how can we blame Marcoux for missing the historical linchpin to the contractarian basis of Shareholder Theory when a scholar of the common law, Austin W. Scott, got it totally wrong, but had the fortitude to write his contagious gaffe into the *Restatement of Trusts*: "Trust creation is perceived as a beneficent transfer of the trust property rather than as a contract."²⁴ Typhoid Mary did less damage.

From this infectious error, one can plainly see that Stakeholder theorists are essentially, unwittingly or not, advocates of Trust Law and so see no need why a contractual agreement between shareholders and stakeholders should stand in the way of Justice when certain conditions apply. Both theories presently stand at the Crossroads in Mississippi. Lucky for them there is a functional equivalency of trusts under contract law which involves 3rd party-beneficiary contracts, thereby offering stakeholder legitimacy under the Shareholder Theory, if and only if they are in fact intended 3rd party beneficiaries.

This contractarian account arises from two fundamental attributes of Trust Law. First, the deal, the shareholder agreement or trust are all volitional. No one can be coerced to accept any legal deal or valid trusteeship. Management makes that key choice to bind themselves to the shareholder agreement. As with any contract, the trust is wholly consensual. The other contractarian feature is that the parties can reject nearly all of trust law. The rules of trust law are applicable only when the trust does not contain terms *au contraire*.²⁵ One chooses trust law by deciding not to oust it. One can agree to almost anything in a Trust. If not, default rules apply. This is the Miltonian freedom, shareholders love, the art and chain of the deal.

All hail the sanctity of choice. "[Property is merely the conventional label for that bundle of economic interests which society deems worthy of protection by law,"²⁶ accordingly, "labeling something property is a conclusion and not a reason. The hard part is not to supply a label but to truly spot the protected interest."²⁷ The combination of consensual formation and party autonomy over the contract terms is essentially the law of contract, and from whence Shareholder Theory is sinewed.

Not so the Stakeholder. Since the stakeholder is not a chosen party to the shareholder agreement and had no autonomous control whatsoever over the shareholder agreement terms, how can they be legally and ethically grafted into the shareholder agreement? The beneficent answer, *viola!*---3rd party beneficiary contract doctrine (Please genuflect). 3rd party-

beneficiary contracts are bedrock to contract law, and for good reason.

One common example of 3rd party contracts involves insurance policies wherein a contract is formed between the purchasing individual and the insurance company, but a 3rd party will receive the insurance payments. When the purchaser of the policy dies, the 3rd party beneficiary legally receives the tax-free insurance benefits and can sue either party (the estate of the deceased and/or the insurance company) if the insurance contract is not upheld. Yet another common example involves the Joint Life with Last Survivor Annuity which when annuitized pays the annuitant, the annuitant and the spouse, or the annuitant and another 3rd party beneficiary until both the annuitant and the spouse have died. These annuities are not term certain, and continue paying out to the annuitant and whoever is designated to receive payments, until both the death of the annuitant and the designated 3rd party. To analogize, the 3rd party beneficiary in both salient cases would be a valid stakeholder under present shareholder theories via the 3rd Party Doctrine within Contract Law.

Of note, there is also a legal distinction between a donee and a creditor as to 3rd party beneficiaries. If a 3rd party beneficiary is a creditor, the contract was entered to discharge some form of debt. Contrasted, donees are given a gift or award under the contract. With life insurance, the policy beneficiary is a donee beneficiary. Stakeholders being grafted into the Shareholder 3rd party beneficiary rubric would have to be donee beneficiaries. This niche within the Shareholder paradigm is more commodious than first imagined, as we shall later see.

The potential legal remedy for a 3rd party beneficiary can vary, depending on the contract and circumstances. Most contracts that involve 3rd party beneficiaries are carefully constructed to protect both parties. At times, a 3rd party beneficiary may have to sue for the contractual benefits. For example, a car passenger in an auto wreck, will oftentimes not get any compensation for pain and suffering unless suit is filed even though legally considered a 3rd party beneficiary of the auto insurance policy.

Third party beneficiaries must be an intended beneficiary. Incidental beneficiaries are excluded from ever attaining status as stakeholders since they are persons who happen to benefit indirectly from a contract and were never intended at contract inception. Law has evolved to more readily perceive customers and employees²⁸ as intended 3rd party beneficiaries than your average Stakeholder Theorists would admit. Sadly, this is more mucky with environmental issues, as we shall see.

being a more credible, more trusted, transparent, inclusive corporate body.

²⁴ Restatement (Second) Of Trusts § 197 cmt. b (1959).

²⁵ Restatement (Second) Of Trusts § 164(a) (1959).

²⁶ Weinrib, E. J. (1975). The fiduciary obligation. *University of Toronto Law Journal*, 1-22; Grey, T. C. (1980). The disintegration of property. *Nomos XXII: Property*, 69.

²⁷ Weinrib, at 11.

²⁸ Providing employees with standing to sue the directors is a core normative aspect of the stakeholder value approach. O'Connor, M. A. (1992). Human Capital ERA: Reconceptualizing Corporate Law to Facilitate Labor-Management Cooperation. *Cornell L. Rev.*, 78, 899.

Even so, it should be quite clear by now that a usable fiduciary duty can easily emanate from a contractual relationships, especially one involving long duration and multistage complexity which makes contracting with precision difficult. Despite the intended end-result being an ironclad contract, a contract remains forever relational whenever parties cannot reduce key terms into well-defined obligations.²⁹ Since asset management necessarily involves uncertainty, the decision-making and actions of the fiduciary cannot be determined in advance?³⁰

When a dispute arises, the court must then engage in grafting, in relational interpretation.³¹ This is when good faith and fiduciary is imputed into a contract, even unto 3rd party beneficiaries (stakeholders) who are by law subsequently "wedded" into the contract.

"The commodious heart of fiduciary administration is to induce the fiduciary to exercise his latitude beneficently."³² The fiduciary's obligations are open-ended and involve: trust, good faith, fair dealing and active concern. This is the light to which all Stakeholder Theorists venture.

And the administration of this living, breathing, relationship is the very core of modern law of trusts, and wholly derived from the duties of loyalty and prudence (also called the duty of care). The duty of loyalty demands the trustee "administer the trust solely in the beneficiaries' interest."³³ The loyalty norm forbids the trustee (management) from self-dealing with trust assets (shareholder's invested capital) and from engaging in conflict-of interest transactions adverse to the trust (corporation).³⁴ There is no tolerance for self-dealing, and when done, the trustee must disgorge the profits to the trust even if the trustee paid market value for the property?³⁵

Most significantly, the duty of loyalty forbids misappropriation and manages conflicts of interest by mandating the fiduciary to behave in the "sole" interests of the principal, which in this case can only be the corporate shareholders. This is exactly why Marcoux conclusively wins his confrontation with Stakeholder Theorists since by law there is no compromise or weighing when it comes to conflicts of interests as far as the duty of loyalty is concerned. It would intestinally gey Marcoux's argument if corporate shareholders and management could

contractually negotiate away the exclusive benefit rule and thereby allow management to consider other interests, such as stakeholder interests, in their corporate decision-making. Marcoux must forever remain unwilling to concede that even the fiduciary duty of loyalty is subject to modification by agreement of the parties.³⁶ If the principal-shareholder gives informed consent to certain self-dealing by the fiduciary-management, the basis for the duty of loyalty's prophylactic rule against self-dealing becomes porous and superfluous.

In this case, management may engage in the specified self-dealing, provided that the transaction is not against the best interests of the shareholder. Yet, both morality and law are quite firm in that there is a mandatory core of management obligation that cannot be overridden by agreement. For example, the shareholder cannot authorize management to act in bad faith.³⁷

Even if the shareholder authorizes self-dealing, fiduciary law provides substantive safeguards, requiring management to comport itself in good faith and deal fairly with and for the shareholder; as well as procedural safeguards, requiring management to apprise the shareholder of the material facts, which means the facts that would reasonably affect the shareholder's judgment, in securing the shareholder's informed consent.³⁸

The existence of such mandatory (non-contractual) rules sorely vexes purist Shareholder Theorists, particularly those who so wrongfully perceive their Theory as that of maximization of profits and subsequently shareholder's stock prices as opposed to the true, correct and proper Miltonian view of increasing long-held dividends³⁹ through long-term profitability. Committed Shareholder Theorists would fume that sophisticated parties do not have complete "Miltonian" freedom of contract to alter the terms of that relationship, despite the fact the

²⁹ Goetz, C. J., & Scott, R. E. (1981). Principles of relational contracts. *Virginia Law Review*, 1089-1150.

³⁰ Cooter, R. D., & Freedman, B. J. (1991). The fiduciary relationship: its economic character and legal consequences. *New York University Law Review*, 66(4), 1045-1075.

³¹ Hadfield, G. K. (1990). Problematic relations: franchising and the law of incomplete contracts. *Stanford Law Review*, 42, 927-992.

³² Weinrib, note 120, at 4.

³³ Restatement (Second) Of Trusts § 170(1) (1959), continued in Restatement (Third) Of Trusts: Prudent Investor Rule § 170(1) (1992). The 1992 volume does not republish the official comments, which remain in force in the 1959 edition.

³⁴ I Austin W. Scott & William F. Fratcher, *The Law Of Trusts*, §§ 170-170.25, at 311-437. (4th ed. 1987-89). The parentheses and its contents are from the Author and not in the original quote.

³⁵ Hartman v. Hartle, 122 A. 615 (N.J. Ch. 1923).

³⁶ Uniform Power Of Attorney Act § 114(b) (2006); Restatement (Third) Of Trusts § 78, cmt. c(2) (2007); Restatement (Third) Of Agency § 8.06 (2006).

³⁷ Uniform Power Of Attorney Act § 114(a) (2006); Uniform Trust Code § 105(B)(2) (2000); Restatement (Third) Of Trusts § 78, cmt. c(2) (2007); Restatement (Third) Of Agency §§ 8.06(1)(a), (2)(a) (2006).

³⁸ Restatement (Third) Of Agency.

³⁹ Every corporation has the inalienable right to define the scope of shareholder influence by excluding from those with short-term investment horizons (day traders, stock-price strikers and the like) from voting and thereby unduly influencing management's decision-making. In this regard, the Leviathan State can at last lend a calloused hand by legally precluding any voting rights from shareholders who hold corporate stock for less than one year and further instituting a capital gains rate for dividends that diminishes each year until it doesn't. Not surprisingly, this needed corporate law would be in line with droit des sociétés français. One long-term share should equal one vote. Strine Jr, L. E. (2010). One Fundamental Corporate Governance Question We Face: Can Corporations Be Managed for the Long Term Unless Their Powerful Electorates Also Act and Think Long Term?. *Business Lawyer*, 66(1). Stiglitz, J. E. (1989). Using tax policy to curb speculative short-term trading. In *Regulatory Reform of Stock and Futures Markets* (pp. 3-17). Springer Netherlands. Summers, L. H., & Summers, V. P. (1989). When financial markets work too well: a cautious case for a securities transactions tax. *Journal of financial services research*, 3(2-3), 261-286.

Milton Friedman curbed such freedom at the point of coercion, deception and illegality. Even Marcoux's usually reliable allies, Easterbrook and Fischel, erroneously asserted that in trust law "[a]ll rules are freely variable by contract in advance."⁴⁰ This poignant assertion is not only faux, but volatile and nuclear. It's the Skull and Bones, redcoat red, blinking-hazardous and pollutive.

Thus, in some critically key aspects Shareholder Theorists have misunderstood their own position. Indispensable fiduciary rules protect the principal and also 3rd party beneficiaries, like customers, who deal with management. And it is these rules de rigueur that adjudicate all applicable interests, shareholder and/or stakeholder, to the point of applicability.

These rules de rigueur are justified since the law assumes a fully informed, sophisticated principal would never bargain them away. For example, Louisiana never agreed to her white-sanded Gulf, her uterine wetlands, or her Catholic Cajun sentiments be swamped in a deluge of British black gold. No more than Louisiana agreed to have invited Katrina or the Brits in their 1st invasion (War of 1812).⁴¹ A particular principal might be fully informed and still want to bargain away something from the mandatory core. But this occurrence would so rare that a prophylactic (if paternalistic) mandatory rule is warranted, particularly when the principal is not sophisticated and fully informed.⁴² By God, pearled oysters, albino alligators, and the glory of aviation: The Pelican: warrant such protection by Louisiana against all who commit lese majeste.

This is why Marcoux brings up the ironclad (paternalistic?) duty of loyalty, and not the duty of care, which is more contextual and less determinative. The duty of care is comparable to the reasonable person rule of tort and on behalf of the beneficiary imposes upon the trustee a duty to act with such care and skill as a man of ordinary care would if dealing with his own property.⁴³ Under the hegemony of these two duties, which comprise fiduciary duty, are many sub-rules of fiduciary administration, such as the duties to furnish information, to keep and render accounts, to minimize costs, to diversify investments,

to enforce and defend claims, and to invest or preserve trust assets and make them productive.⁴⁴ All these sub-rules are subsumed under the duties of loyalty and prudence by which the beneficial interest is vindicated.⁴⁵

Simply put, if the duty of loyalty is part of the mandatory core, (ironically from Trust Law and hereby used by Marcoux to advocate Contract Law), Marcoux by both Trust Law and Contract Law accomplishes his sought after coup d'etat against hegemonic Stakeholder Theory. But if this core can be modified/tweaked from "sole" interest to "best" interest of shareholders, then Marcoux is no longer invincible, no more. a god. His hair is cut and he is cast down. Marcoux knows this, which is why he clings to the duty of loyalty (one of the two components of fiduciary duty) that by law must be in the sole and exclusive interests of the shareholders. A best interest rule is the sharp Damoclean sword hanging by a horse hair above Marcoux's revolutionary head.

A Fiduciary Breach Resulting In A Serious Harm Emblazons The Morality Paradigm: Stakeholder Theory.

Who can deny that a serious breach of fiduciary duty can be a gruesome sight, and stakeholder literature abounds with nigh-infinite examples (Enron, Maddoff, and so on). Not surprisingly, Courts naturally use moralistic language to describe such behavior. Even Marcoux gives in to this unnecessary moralizing (as does this hypocritical Author throughout the endnotes. It's hard to refrain when you really care. God forbid, love.) Even though fiduciary duties are and should be contractually assumed since they codify the appropriate behavior for a corporate shareholders and management. But Courts, stakeholder theorists and at times Marcoux's sermonizing about fiduciary duties can distract them from paying sufficient attention as to whether and why someone is actually a fiduciary and what fiduciary standards applies under the circumstances.

Stripped of legalistic formalisms and moralizing rhetoric, the *raison d'etre* of the fiduciary obligation is deterrence.⁴⁶ The agent (corporate management in this case) agrees to act in the principal's best interests by the threat of suit if failing to do so. The agent is given expansive powers, but must exercise that discretion in the principal's best interests on pain of suit and disgorgement remedies. Viewed in this manner, the operation of the fiduciary obligation becomes intuitive.

Marcoux's two most stalwart allies, Easterbrook and Fischel, emphasizing corporate law,

⁴⁰ Easterbrook, F. H., & Fischel, D. R. (1993). Contract and fiduciary duty. *JL & Econ.*, 36, 425, 432. Prevailing trust law is to the contrary. Restatement (Third) Of Trusts § 78, cmt. c(2) (2007) ("[N]o matter how broad the provisions of a trust may be in conferring power to engage in self-dealing or other transactions involving a conflict of fiduciary and personal interests, a trustee violates the duty of loyalty to the beneficiaries by acting in bad faith or unfairly."); Langbein, J. H. (2003). Mandatory Rules in the Law of Trusts. *Nw. UL Rev.*, 98, 1105.

⁴¹ The preservation of Her wetlands reign supreme since, as most ornithologists are fully aware, the wings of Noah's dove were Pelicanic.

⁴² The exclusive benefit rule emanates from Trust Law, and yet Marcoux and this Author advocate for a contractual (Shareholder) view. Marcoux and this Author are using a bedrock of Trust Law (stakeholder) to put stakeholder theory, as presently explicated, to perpetual rest. Oh well.

⁴³ The applicability of which to investing and managing the trust assets appears in Restatement (3rd) of Trusts: Prudent Investor Rule §227 (1992).

⁴⁴ Restatement (Second) Of Trusts §§172-78, 188 (1959); Restatement (Third) Of Trusts: Prudent Investor Rule §227(b) (1992).

⁴⁵ The duty of impartiality, which is merely an application of the duty of loyalty, requires the trustee give due regard to the interests of all beneficiaries with no preference to one over any other. Restatement (Second) Of Trusts §§183, 232 (1959).

⁴⁶ Easterbrook, F. H., & Fischel, D. R. (1981). Corporate control transactions. *Yale Lj*, 91, 698.

ably explain why fiduciary law is not morality based, not Trust Law based, but rather, agreed-upon, contractarian: When the task is complex, and contractual efforts will span a substantial time, a detailed contract would be ludicrous. When one party hires another's money-making skill set, there is not much they can write down given the future's refusal to be predictable. Thus, in lieu of specified clauses, the management of corporations or the trustee of a trust takes on a duty of loyalty and a duty of care (prudence in Trust Law). The process is contractual since both principal and agent enter the agreement for profit.⁴⁷ At the end of the day, properly defined a fiduciary relation is a contract characterized by an inability both to specify exactly, future behavior and to effectively monitor, that profit-making behavior.⁴⁸

As Marcoux is so subliminally aware, the duty of loyalty supersedes trumps and outright replaces detailed contractual terms. To great effect, Marcoux makes this exact same point by properly citing Easterbrook on page 13.

And now we must journey to where true and appropriate stakeholders can safely reside within the Shareholder rubrics: contract law's 3rd party beneficiaries. Nearly all Marcoux's, Stakeholders', and this Author's moralizing can all be rightly subsumed within the contract doctrine of a 3rd party beneficiary: a person can acquire the right to sue, despite not having been an original or active party to the contract. This is where Stakeholders must plant their flag, and no Shareholder can take that fort if and when the doctrine applies.

This right vests when the 3rd party assents to the relationship. The 3rd party then either sue the contract's promisor (*promittens*, or the performing party, management) or the promisee (*stipulans*, or anchor party, corporation), depending on how and why the original contract relationship was created. In conformity with Marcoux's Roman Basis of fiduciary duty, this principle too is so grounded and is known as *ius quaesitum tertia*. Any agreement, accord, or contract made in favor of a 3rd party is known as a 3rd party beneficiary contract (*stipulatio alteri* or *pactum in favorem tertii*). Any subsequent action to enforce a *ius quaesitum tertio* is a 3rd party action. From this base, we can now explore the stakeholder's most profound example of an injustice needing corporate governance redress, and see said grave injustice fits reasonably snug within the realm of 3rd party beneficiary.

Pristine Example of an intended 3rd Party Beneficiary Stakeholder Lawsuit Involving Fiduciary Duties that Stomp, Throttle and Drown Shareholder Interests

In this Ideal Example (Plato), BP leased from Transocean the *Deepwater Horizon* drilling platform

with which to drill off the Louisiana coast. On April 20, 2010, some 40 miles off the Louisiana coast the exploratory well blew out, creating the greatest oil spill in human history. Oil spewed from the seabed 5,000 ft. below at roughly 25,000-30,000 barrels per day.⁴⁹ In this wake of sludge, 11 homo sapiens were dead, 17 injured. The cortege of which is ongoing.

Various attempts to stem spillage failed. The every widening darkness crept upon once transparent waters and the Devil's Blood seeped into depths no man had ever ventured, valuable muck suffocated marine life and water birds, estuaries became flightless, and shores seeped black gold until enough Cajuns ventured deep into their souls, bid their wives adieu and raised the **Skull and Bones**.

The National Oceanic and Atmospheric Administration shut down recreational and commercial fishing in a huge portion of the Gulf, while the federal government issued a 6-month moratorium on exploratory drilling, thereby idling about 33 drilling operations in progress.⁵⁰ Meantime, after meeting with President Obama, BP quite reluctantly agreed to a concordat and set up a \$20 billion compensation fund.⁵¹ Reportedly operating on a self-insured basis, BP carried little to none 3rd party liability insurance.⁵² Given the minimal insurance, BP's pockets are perhaps not deep enough to meet the overall liabilities which, in addition to the \$20 billion compensation may well include \$21 billion in further civil fines via the Clean Water Act (CWA).⁵³ Stakeholder litigation followed like a force majeure, and the Lord was with them...and even the angels shall forever wonder if BP had so defecated in the North Sea, or effected the Thames instead of Old Man River, would their response have been so aloof, so nonchalant, so Thackerian, so crumpet and tea time, so sang-froid instead of cafe u lait and beignets

⁴⁹ Gillis, J., & Fountain, H. (2010). New Estimates Double Rate of Oil That Flowed Into Gulf. *The New York Times*.

⁵⁰ Bill Sasser, *Despite BP Oil Spill, Louisiana Still Loves Big Oil*, Christian Science Monitor, May 24, 2010, <http://www.csmonitor.com/USA/2010/0524/Despite-BP-oil-spill-Louisiana-still-loves-Big-Oil>.

⁵¹ Deepwater Horizon Oil Spill Trust (Execution Copy) (Aug. 6, 2010), http://media.nola.com/2010_gulf_oil_spill/other/Trust%20Agreement.pdf.

⁵² This fund operates independently of the Oil Spill Liability Trust Fund, which is funded by taxes on oil exports and imports into the US, was inadequate to redress the BP spill since it merely requires a responsible party like Deepwater Horizon to produce proof of "financial responsibility" up to \$150 million either by insurance, surety bond, letter of credit, and/or qualification as a self-insurer. 33 U.S.C. §2716(c) and (e)(2006). Transocean reportedly carried \$500 million in physical damage insurance and \$900 million in 3rd party liability insurance. Howard Epstein and Theodore Keyes, *BP Oil Spill: An Insurance Perspective*, N.Y.L.J., Aug. 18, 2010, available at http://www.srz.com/Epstein_Keyes_NYL_BP_Oil_Spill/.

⁵³ In 2010, the Justice Department sued BP to retrieve fines and penalties from violating OPA. See Jerry Markon, *BP, 8 other firms sued by Justice Dept. over gulf oil spill*, WASH. POST, Dec. 15, 2010, <http://www.washingtonpost.com/wp-dyn/content/article/2010112/15/AR2010121503894.html>.

⁴⁷ Easterbrook, F. H., & Fischel, D. R. (1993). Contract and fiduciary duty. *JL & Econ.*, 36, 425.

⁴⁸ Easterbrook, F. H., & Fischel, D. R. (1993). Contract and fiduciary duty. *JL & Econ.*, 36, 425, 426-27.

wolfed down by sans-culottes declassé livid to set free the vampires of La Nouvelle-Orléans.⁵⁴

On 12 May 2009 at a postgraduate lecture to Stanford Business School, perhaps in a not so subtle attempt to merge Yin and Yang⁵⁵ poseur Tony Hayward⁵⁶, chief executive of BP, stated to the business attendees, "...our primary purpose in life is to create value for our shareholders. In order to do that you have to take care of the world." Apparently, the Gulf of Mexico, notre eau de vie, and the surrounding environs are not part of the World.

Pure "economic loss" is the kind of loss that strikes the wallet and nothing else. A party suffering only economic harm recovers damages solely founded upon a contractual claim as opposed to one grounded in a tort such as negligence or strict liability. Sadly, this legal shield⁵⁷ against tort liability is strikingly ineffective in connection with oil spills. There the overwhelming harm is not to human lives and private property as such but to "unowned resources," viz. the high seas, territorial waters, wildlife⁵⁸, and marine and coastal environment, all of

which lie in the public domain. Since these resources are publicly owned, a private claimant is typically unable to recover on the basis of direct property loss, or even able to attach his economic losses to any physical loss, even parasitically speaking. This is an example of a 3rd party beneficiary who is a valid Stakeholder.⁵⁹ Where private claimants do not have access to remedy a wrong, the Stakeholder theory/3rd party contract beneficiary should take root and form.

The public resources are exogenous to the private property law system and therefore the "damage" consists mostly of pure economic loss. For example, marina owners and seafood processors who depend directly upon these public resources for their livelihood are in theory barred from recovery. This would adversely affect the menu of chez Galatoire's, and obviously that's not going to happen.⁶⁰ Thus, in the end, Stakeholder Theory won, when the Sovereign State of Louisiana⁶¹ defeated the Brits (BP), thereby winning the Second Battle of New Orleans⁶² where once the very Redcoats who defeated Napoleon lost to the ruffraff of New France. Here are BPs terms of surrender of which both General

⁵⁴ Man perceives New Orleans as a City of Sin. Quite the opposite. Fact is, vampires, werewolves, fallen angels and more do reside in the City that Care Forgot, but they all have one peculiar distinction. Each and every ghoul has asked God for forgiveness. And to there, He sends them even though they cannot be forgiven, for the blood of Christ is only applied to man. Problem is, vampires, demons and such, on occasion fall off the wagon and imbibe in the draining of humans of all their blood, flesh or spirit, depending on the particular appetite involved. And then, the guilt sets in, there's the requisite visit to the parish confessional, who sends them onto their various Chapters of Anonymity (e.g. Vampires Anonymous, Noisy Spirits in the Vieux Carre' Anonymous and so on. And yes, each ghoul gets a medallion at the appropriate benchmark.) Point is, New Orleans is not the City of Sinners. It is the City of generally repentant Vampires and Whatnot. To fairly compensate the human New Orleanians from the occasional hauntings, half-eaten bodies, Vampire feedings (most often Dirty Birds or 49ers, so no real foul), and so on, the Lord in 1967 through his mouthpiece, the Archbishop, publicly made his Team, the Saints, an allusion to November 1 being All Saints Day in the Catholic Faith. The Lord failed to mention most Saints were martyrs, which aptly explains the Wilderness Years.

⁵⁵ "Entrepreneurial Spirit Needed". Stanford Business School via Stanford University. 12 May 2009.

⁵⁶ If you look into the bathroom mirror and see Marie Laveau, please, please blame me. Being both an avid practitioner of Catholicism and Voodoo, Marie has friends in locales high and low. Hire a retiree from MI-6 and verify that her mausoleum in St. Louis Cemetery No. 1 at 3421 Esplanade Ave is wide open. No one knows who took axe and pick and set her dank spirit free (it was me!), but to you her spirit alights. If you notice a woman behind Marie, it's Mme. Marie Delphine Lalaurie, like yourself, by every societal standard sweet, kind and most importantly, captivating. Good luck in your new life: the Grand Guignol!

⁵⁷ By contrast, economic loss does include damages for disappointed expectations, such as lost profits, the benefit of the bargain lost, and the reduced value of property. Throughout the United States, the economic loss doctrine is recognized to a certain extent by courts but not in any sort of uniform fashion whatsoever.

⁵⁸ The ownership and title to all wild birds, and wild quadrupeds, fish, other aquatic life, the beds and bottoms of rivers, streams, bayous, lagoons, lakes, bays, sounds, and inlets bordering on or connecting with the Gulf of Mexico within the territory or jurisdiction of the state, including all oysters and other shellfish and parts thereof grown thereon, either naturally or cultivated, and all oysters in the shells after they are caught or taken therefrom, are and remain the property of the state, and shall be under the exclusive control of the Wildlife and

Fisheries Commission La.Rev. Stat. Ann. §56:3(A) (West 2011). "The control and supervision of the wildlife of the state, including all aquatic life, is vested in the Louisiana Wildlife and Fisheries Commission." La. Const. art. IX, §7(A).

Louisiana courts also have recognized the state's constitution created a public trust for the protection and conservation of its natural resources. See *Save Ourselves, Inc. v. La. Envtl. Control Comm'n*, 452 So. 2d 1152, 1154 (La. 1984) (citing La. Const. art. IX, §1. And so, Louisiana is a viable stakeholder since as owner it has the requisite property rights. Also, one must assume that BP intended Louisiana not suffer extreme wetland and wildlife damage when effectuating its shareholder agreement. Thus, Louisiana is a valid 3rd-party beneficiary in the BP Gulf Spill debacle, and not some incidental objet trouve.

⁵⁹ As a consequence, where corporations are found to have violated environmental regulations, the share price losses amount only to the regulatory fine in contra-distinction to product recalls which harm corporate customers with correlative share price losses commensurate with the discovered damage. The market is not effective in punishing corporate environmental failure where the primary damage is against external 3rd parties. Karpoff, J. M., Lott Jr, J. R., & Wehrly, E. W. (2005). The Reputational Penalties for Environmental Violations: Empirical Evidence*. *Journal of Law and Economics*, 48(2), 653-675.

⁶⁰ 209 Bourbon St, New Orleans, LA 70130. Galatoire's specializes in French Creole cooking. Perhaps as an embodiment of the egalitarian French Revolution (1789), exceptions to their first-come-first-served policy have never been allowed. According to the restaurant, President Ronald Reagan called U.S. Senator J. Bennett Johnston, who was waiting in line for a table. After taking the President's call, Senator Johnston returned to his position in line. Of note, Author Tennessee Williams was a habitué and preferred to sit by the main front window looking out onto Bourbon St. As such, Galatoire's is rightfully mentioned in: *A Streetcar Named Desire*. Much as I would look onto Boubon for décolleté of each and every coquette. *Laissez les bons temps rouler!*

⁶¹ In 1803 Louisiana was 828,000 square miles, and crucified Herself so that other sovereign States (15 States and 2 Canadian Provinces) might come into Existence. Had Louisiana maintained a more independent and Texan point of view, She would have had the electoral votes to perhaps have been more rightly treated by this Nation after both the BP debacle and Katrina. But now, with merely 3 electoral votes, what can an Old Mother, or Old Man River for that matter, rightly expect? How quickly this World forgets.

⁶² Upon any verbal or inscribed mention of BP, at His command, the 6-winged Seraphs immediately stop chanting their Holy, Holy, Holy...and sing with all their invisible hearts Johnny Horton's number #1 1959 hit, 'The Battle of New Orleans.' Amen.

Jackson and this Pirate Jean Laffite are so proud: http://seafoodsustainability.us/uploads/MOU_LouisianaBPoilspill.pdf.

One must keep in mind that a 3rd party beneficiaries' legal right arises only if the purpose of the contract was to benefit a 3rd party who either relied upon or accepted the contract's benefit. "Clearly", BP intended to not destroy the very State of Louisiana, and Louisiana relied on this by allowing BP to drill so near Her children, her pod of chicks, fed by the very red blood from her own pelicanic breast (for verification please closely review the Louisiana State Flag).⁶³

Had Louisiana known BP would willfully be so under-insured and unprepared to fix a drilling explosion, which is a foreseeable risk, Louisiana would have prevented BP from doing business near her shores, her wetlands, her fisheries, her noble Cajuns. Thus, Louisiana was an intended 3rd party beneficiary who detrimentally relied on BP's good faith. BP consistently violated its fiduciary duty to Louisiana, for which BP was not punished near enough. This result fits neatly within the Shareholder Theory, which is contract-based and more specifically in this case, adequately addressed by a 3rd party beneficiary paradigm. Thus, more cases than initially surmised would fit within this Shareholder purview, particularly when long-term maximization of company value is the decisional goal of management and not short-term profits⁶⁴ or mere increase in the price of company stock price. This one-two combination should bring a lasting and suitable detente in the not-so Cold War between Shareholder and Stakeholder Theorists.

A near-constant 3rd party beneficiary would be shareholders-managers' customers since no one could truthfully argue their customers were not an intended beneficiary at contract inception. Thus, the preeminent 3rd party beneficiary (stakeholder) would be the customer and no customer more so than the insured (policy-holder) with a mutual life insurance company where they are no shareholders, only policy-holders. In that case, the customer (the

insured) is both the "shareholder" and "stakeholder," such a person would be in the proverbial "catbird seat."

It is understood that shareholders via their management intend to do business with the public-at-large for a profit. And so the public is nearly always a 3rd party beneficiary since it was in mind as an intended beneficiary when the shareholder agreement was made between shareholders and management. Obviously, no company can get a public license to intentionally harm the public, and so to do business with the public, whether by C-corp status or even a DBA, the public and more specifically, the customer is presumptively a 3rd Party Beneficiary. The question remains on whether the State can swoop in and defend these customers. The answer is of course. It has, and will continue to do so. In encouraging BP to establish the 20 Billion dollar trust fund (a stakeholder fund, a 3rd party beneficiary fund), the Federal Government dipped its hand in the water to quell the uproar in public opinion. But as with all such funds, the final beneficial effect will be largely determined by claimants' utility curves and the time value of money. And who can forget the lengthy *Exxon Valdez* litigation only to have the U.S. Supreme Court restrict the scope of punitive damage awards.

Admittedly, what happens when the rubric of 3rd party beneficiary is perhaps insufficient since ironically, a Trust (stakeholder) structure could have been used in the BP situation to great effect? Claimants are attracted to courts of law because, among other things, of the individual attention given to them. Claimants seek courts to get a personal, thorough review of their case. At times, neither the Courts nor Contract Law are equipped to handle a case like this wherein multiple State were nearly engulfed by hurricanic losses.

But a Trust structure, which does embody Stakeholder theory, could employ special procedures and case management tools in order to have the Trust Fund operate in an orderly and efficient manner. If the Court is required to sort through beaucoup de individual claims (over 100,000) to determine just claims from unjust ones, Justice grinds to a standstill in all of Louisiana. In this instance, the stakeholder theory, Trust Law, would perhaps have led to lower agency costs, better services, and better compensation. When the legal system cannot justly remedy the problem, stakeholder theory reasserts itself, even though the presumption for a wealth-creating society must tow the Shareholder Theorist line of thought and being, even if tears must cascade behind the eyes and down the throat.

Control and Information Vulnerabilities

In A. Control and Information Vulnerabilities Revisited, Marcoux wastes ink and tree persuading

⁶³ In Act 3, Scene 4, did not King Lear cry out: Death, traitor! nothing could have subdued nature

To such a lowness but his unkind daughters.

Is it the fashion, that discarded fathers Should have thus little mercy on their flesh?

Judicious punishment! 'twas this flesh begot

Those pelican daughters. (Act 3, Scene 4)

The daughters, Regan and Goneril, betray King Lear only after he has given them all his land and power. King Lear is that mother pelican who pierces so deeply her own breast that might greedy daughters thrive.

As is plain, when the Bard walked the Earth, mother pelicans were thought to have pierced their own breasts so their young might drink the richest sustenance. Just before Shakespeare wrote *King Lear*, the barren Queen Elizabeth I portrayed herself the pelican, that so self-sacrificing "mother" to her "children" (the subjects of England). Perhaps this is poetic indicia that not all Lordly Brits deserve to be actually drawn-and-quartered.

⁶⁴ Jacobs, J. B. (2011). Patient Capital: Can Delaware Corporate Law Help Revive It. *Wash. & Lee L. Rev.*, 68, 1645.

the reader shareholders are deserving of fiduciary duties. There is no such need. Contract Law amply provides for fiduciary duties. They are ably imputed into any contract by at minimum the covenant of good faith and fair dealing, which also applies to intended 3rd party beneficiaries of the agreement. The query is not whether shareholders are entitled to or owed a fiduciary duty; but rather, does such an obligation inhere to anyone else, namely a Stakeholder that could not come under the rubrics of intended 3rd Party Beneficiary. The answer, is the almost always, No. Contract Law, not Trust Law, generally is broad enough to protect all victims. A possible exception would be the BP Gulf Spill, but even there a 3rd Party Beneficiary analysis would suffice, but a Trust (Stakeholder) in that case would probably have been more efficient and more just. Courts adjudicate Contract Law always, but in special cases, Special Administrative Bodies would probably be more proper to adjudicate and process claims, particularly in Class Action cases or where only the State is the owner of what was damaged or seriously harmed (Gulf of Mexico, wildlife, the menu of Galatoire's (specifically, crab sardou: hollandaise sauce over lumps of white crabmeat, artichoke hearts and a verdant spinach en creme de la creme)).

B. Reply: The Ready-Market-for-Shares Argument

In this Section Marcoux literally thrashes Stakeholders Theorists who so glibly assert shareholders are protected against managerial practices adverse to their interests in a way that employees are not, since they may easily dispose of their shares and recoup the current market value of their investment. If Marcoux were more right on this point we would all have to bend the knee and declare him a demi-god. His analogy that the existence of a market for shares is no more a protection of shareholders' investments in their firms than is the existence of wrecking yards a "protection" of car owners' investments in their cars is more than incisive. This argument reaches the level of a Platonic Ideal withering the ideological myopia of Stakeholder Theorists who leap at any argument that makes the employee the defenseless victim the way a dog bolts after a bouncing ball.

While fearing to mar Marcoux's chef d'oeuvre in this section, I would only add that employees have many legal remedies available to them. And as for retraining employees when a firm leaves, it is up to the government, State or Federal, to retrain it citizenry (if they truly believe in them since they are its tax base in perpetuity. Firms, as with the State and Federal government are Immortal (carte blanche) and employees are not their source of revenue en perpetuity: Immortal corporations, enabled by Nordiste law live en perpetuity.) It is not the moral or legal obligation of a firm to have its one-time

employees trained for life--a manifestation of loyalty that ironically, the employees themselves would never render the employer. An employee can leave for higher pay and be considered smart, dutiful to his family and so on, but a firm that leaves to survive due to the Nigh Almighty Invisible Hand is per se to be a scumbag. This Stakeholder position seems to be one of at least two faces.

To his credit, Marcoux has one face, which admittedly at times is hard to face emotionally, or with a keen sense of social justice. But to oppose him effectively you must face his unique face creatively. No one has done that yet.

In this Section, one can only join Medusa as a sister femme fatale, or face Marcoux and be turned to stone. Every Section before this one was just venomous hissing, an act of mercy, a warning, a cue to run for your life. His enemies will say Section 3B. was a trap, but deception (and illegality) is precluded by Marcoux. This Game has hors de combat, some fatal, but it is more fairly played than surmised; and when not, the State if true, does more than referees, it rectifies⁶⁵. So who is to Bless, and who is to Blame?

Has anyone even bothered to ask Marcoux-Medusa if he/she wanted to turn even one person into stone? One running boy into an immortal statuette of playfulness? Granted such face- to-face time could be lethal. But when you save every seal and starve the killer whales, when you kill every lion to protect every antelope, when you castrate every male in the name of humanity, when you prevent profit and thereby prevent loss, you my enemy will have spoken face-a-face with Medusa-Marcoux and survived.

IV. The Manager- (Non-Shareholding) Stakeholder Relation, B. Customers.

In the last paragraph of IV. The Manager-(Non-Shareholding) Stakeholder Relation, B. Customers, Marcoux errs big-time in stating, "customers exhibit only limited control vulnerability, but generally lack information vulnerability." In the late 1950s and early 1960s, Thalidomide was a widely used to assuage nausea in pregnant women, the side effect of which caused severe birth defects in thousands of children. And yet thalidomide has never been successfully banned, and rightfully so since its benefits outweigh its costs as to leprosy and later, multiple myeloma. Eventually, with an improved understanding of these molecular targets, safer drugs may be designed. But even so, the public uproar was well-founded, justified and fortunately triggered a turning point in developing systematic toxicity testing protocols. Not to mention the use of thalidomide as a tool was a key

⁶⁵ Who can deny that the stock market is a very selfish policeman who only inflicts penalties on corporations whose actions only have damaged the corporation itself. Where the corporation has damaged other Louisiana or the Gulf of Mexico, then far from penalizing it, the stock market might even reward GP for enhancing its profits from its "effective cost-cutting", at least prior to being exposed to regulatory discipline and public censure.

in developmental biology which has led to important discoveries in the biochemical pathways of limb development. Marcoux, what costumer in 1960 could possibly have known a scintilla of this!? Not even a customer such as Marie Pasteur would not have fathomed the effects of thalidomide on her unborn Jean Baptiste.

Marcoux's assertion in this Section only applies to products which are both manufactured and commoditized (widgets), which in this information age is less and apropos for analogous usage. It is because companies failed miserably to disclose key nutritional information to their autonomous soul-imbued customers that this Nation found it necessary to not stop merely refereeing the Game, but step in, throw the flag and assess a new cost/rule via the Nutrition Labeling and Education Act of 1990 (NLEA) which provides the FDA with specific authority to require nutrition labeling of most foods regulated by the Agency. The Stakeholder Government quite arguably has a moral right to do this, as in nigh any case wherein there is no informed consent, thereby turning customers into pure means by negating their inherent soul-imbued infinitude. This must never go unaddressed, and the stakeholder-esque zebras got it right. Now huddle up, cuz the clock is, like always, running...At the whistle, the best Game to create societal wealth, must and will go on...in Russian or Chinese, but preferably English, that amalgamated langue de Normans, Saxons, Angles, Jutes and yes, Brits.

Shareholder Theory As It Should Be and Not As Usually Stated

Perhaps even Marcoux misstates Shareholder Theory as best stated. Maximizing shareholder value as the ultimate goal is not completely consistent with the intentionality of viable or proper shareholder theory. Shareholders receive a return from their invested capital in two different ways: 1) dividends paid out by the corporation and 2) increased share prices.⁶⁶ As mentioned earlier, Milton Friedman's September '70 article "The Social Responsibility of Business is to Increase its Profits," is the very basis of Shareholder Theory and made clear that the *raison d'etre* of corporate governance was to increase dividends through long-term profitability; rather than, merely or solely increase share price in a possibly irrational stock market. And so, true Shareholder Theory never utilizes market returns as the primary end state. On page 13, Marcoux never alludes to dividends en perpetuity to better justify why managers owe shareholders a fiduciary duty. Unfortunately, Marcoux might have greatly bolstered his position if he had.

⁶⁶ And if one comports with a semi-efficient or efficient view of the market, such revelations come swiftly much of the time, although the market information failures are notable (Enron, Maddoff and so on).

Let us pray we never forget those notable instances when corporate management acted in a manner more for their rapacious selves than the trusting shareholders. Enron Corp. CFO Andrew Fastow created a partnership bankrolled with Enron stock and comprised of very risky ventures, and stood to easily make millions even if Enron lost money on the deal. And in fact, Enron lost more than \$500 million from these management misdeeds and entered bankruptcy.⁶⁷

Also, while Kenneth Lay of Enron and Scott Sullivan of WorldCom Inc., profited big-time from bonuses and stock options while their shareholders' capital was disappearing, Shareholder Theory would find such behavior despicable, since management should act only and exclusively in the shareholders' interests. This is why any form of self-dealing by management is clear breach of duty of undivided loyalty, and so how can management consider, hear, or entertain any stakeholder viewpoint under this paradigm. That's why by (Trust) law, Marcoux lands his coup de grace, and wins big.⁶⁸ This is bien pensant by Marcoux.

But for now, despite this defensible argument, Shareholder Theory throughout numerous journals is being repeatedly tarnished by association. Various authors seemingly, more concerned for emotional resonance instead of clarity or partial solutions, have spray-painted the greed of certain infamous corporate managers onto not only Shareholder Theory in general, but unto all who would believe in or espouse said Theory. Not finished their graffiti, Stakeholder Theorists then spray-paint throughout their vast literature this particular blase straw man: that Shareholder Theory justifies and mandates any deed if in pursuit of shareholder returns. As to this Marcoux comes to the rescue, noting that Shareholder Theory demands profits be acquired legally and without deception. There is no grace granted this sort of overt illegal behavior discovered in too many financial scandals au courant. Not one single, solitary corporate executive who, either broke the law or mislead employees, operated within the confines of Shareholder Theory. Thank you, Marcoux for at long last shattering that nefarious crucible.

⁶⁷ Behr, P., & Witt, A. (2002). Visionary's dream led to risky business. *Washington Post* (July 28).sec. A, p. 1

⁶⁸ If under contract law, corporate management had to act in the shareholder's best interest, but not necessarily in their sole interest, Marcoux's ship would suddenly be taking on water. But under present fiduciary law based on Trusts, a corporate manager breaches their fiduciary duty by taking any action in the best interest of the stakeholders or themselves whenever the action benefits stakeholders or themselves, and not exclusively the shareholders. This disregards modern corporate governance reality. And so, the Courts wedge in some fudge as an exception that states by law, incidental self-serving is allowed. Yet who in their right mind thinks executive bonuses are incidental? The Courts' suspension-of-disbelief notwithstanding, the sole/exclusive interest rule de juris unconditionally promulgates that all conflicts of interest inevitably imperils the sole interest of the corporate shareholders. Marcoux makes fantastic use of this current law to land a coup de maitre against Stakeholder Theory.

Another straw man Stakeholder Theorist use with morbid regularity is that since corporate management is charged with maximizing shareholder value and are paid large incentives to accomplish this through stock options or other schema, they can be expected to engage in whatever manipulations are necessary to attain that goal. And furthermore, if those manipulations mean setting up illegal ventures and then shredding any incriminating evidence, Shareholder Theory will insert the morality of OUGHT into that genre of behavior, assuming the Nixonian managers don't get caught. Both Courts and our societal milieu would find these actions despicable and since shareholder theory "drove" management to behave his way, Shareholder Theory is bankrupt and must be cast into the dustbin of History. This yellow journalism is in the end, a voluptuous succubus.

Conclusion

We are allegedly witnessing the emergence of a society predominantly based on fiduciary relations. Today, affluence seems best generated by interdependence, but supposedly personal freedom is cherished at all times. More and more, society disavows the Courts and turns to an arbitrator, the (usually federal) government, for protection from any perceived abuse by those depended upon for specialized services or products with hidden complexity or containing known or unknown affects either in the short or long-run.

A fiduciary society, for better or worse, does not focus or reward competitive-conflict, and the fruit attained thereby from the Invisible Hand; but rather, harmonious integration of interest validated within a highly regulated, Kantian schemata: does evermore more compliance lead to evermore Justice? This New Age permits the government to moderate between altruistic goals and all-too human desires, as well as between the Scylla and Charybdis of increasing societal welfare while corralling the will-to-power (amour propre) that wants to get more than a "fair share." All mighty charioteer Apollo, where art thou? For what you do, the Federalists promise to do 24/7. Beware of what ye ask for, Phaeton. You, mortal man, will only control the dark steeds of Apollo by compliantly, killing them. No heart but Christ can beat l'Etat, c'est moi!

There was a time when chief executives perceived themselves as overseeing customer and employee welfare. If each year the company took in reasonable profit and bumped up dividends: wife, kith, kin and all those around critically acclaimed your succes d'estime.⁶⁹ But before too long, shareholders observed the ever-increasing cost in the shareholder-management relationship, noting that high-level managers did not maximize profits unless shareholders poured both more capital into incentive

packages and better measured-monitored the results. To make matters worse, managers believed that if they did not vigorously beat the Shareholder Drum of ever higher profits, they might soon very well find themselves, unemployed. Although as Ellsworth noted, "If corporate management fulfills their dual duties of care and loyalty, the courts do not overturn, or even seriously review, their decisions," even if those decisions arise from stakeholder theory tenets.⁷⁰ Yet if managers do not maximize profits, and boards do not remove them, the corporation's underperformance will be noted in the marketplace, and eventually be subject to hostile takeover: both the board and the managers replaced by those most likely to detect such underperformance: Robber Barons.

Unfortunately, as you can see, reasonable applications of either theory can easily yield qualitatively different obligations on corporate management. Too often, any causative linkage between such acted upon obligations and the Profit & Loss statement is simply not there or too indirect to really matter. The theory that can throw out the bathwater and keep the baby will win. Ultimately, this Author adheres to the modified Shareholder Theory elucidated herein while admitting that the Human, All-Too-Human Stakeholder Theory evinces every fiber of our moral being when injustice harms that which we most love.

Once Shareholder Theory holds to long-term maximization of company value for the Shareholder, and Stakeholder know themselves to generally be 3rd Party Intended Beneficiaries then while admittedly, one theory becomes moonlight contre-jour, the other shall no longer dream dreams that cannot fly. See for yourself. BP's shareholders presumptively never intended to ruin the Gulf of Mexico and the Piratical City of God; and so, once ruined by BP, said Shareholders are beholden to those (intended) 3rd Party Beneficiaries so affected. Perhaps, shareholders of sufficiently large publically held companies are morally obliged to band together as an industry and establish a fund through insurance (or re-insurance) for harmful outliers that are rare but when they occur causes serious harm to either the surrounding area (stakeholder) or any other probable (stakeholder) 3rd party beneficiary.

One can see why Stakeholder Theorists sense the denouement of Shareholder Theory, and some already declare it ancien regime. Apercu, scandals at Enron, ImClone, Tyco International and WorldCom, not to mention national concerns about the objectivity of accountants hired to audit financial statements, or the type of incentives at Credit Suisse First Boston or investor recommendations at Merrill Lynch have been a rich compost to usurp shareholder supremacy.⁷¹ This Article has made clear that these

⁶⁹ Cassidy, J. (2002). The greed cycle. *The New Yorker*, 23, 64-77.

⁷⁰ Ellsworth, R. R. (2002). *Leading with purpose: The new corporate realities*. Stanford University Press, 348.

⁷¹ Corporate accounting scandals were also involved at Polly Peck, Xerox, Royal Ahold and Satyam.

scandals reveals the moral paucity of that company's management and is not conclusive evidence of any Vampiric qualities inherent to either shareholders or their life-rendering Theory. And this Article has hopefully also made clear that Stakeholder Theory is best attainable within the legal rubric of 3rd party beneficiary analysis. But of course, there are exceptional exceptions which not only should remain just that, exceptional exceptions, but like lord Voldemort, never be discussed, named or mentioned until met vis-a-vis. *Honi soit qui mal y pense!*

Despite presently in an awkward position, Shareholder Theory has the advantage of being right, even if it desperately needed this Article to save itself. Stakeholder Theory simply cannot on a consistent basis be applied at a societal level without instituting at minimum a highly regulated (straight-jacketed?) society. This is the partial legacy of Kant's Imperative and the "Enlightenment" of 1789. To make matters worse, Stakeholder Theorists too often misrepresents Shareholder Theory as urging managers to "do anything you can to make a profit," when said theory obligates managers to increase profits only through legal, non-deceptive means.⁷² Second, some see shareholder theory as solely geared towards short-term profit maximization at the expense of the long run. However, a more viable Shareholder Theory would incentivize Shareholders to develop long-term horizons so their interests would be significantly more aligned with stakeholders, especially employees. Having dividends payout a higher rate of return based on a sufficient holding period, along with a capital gains tax rate diminishing over a longer holding period, would better enable corporate management to inculcate a long-term paradigm⁷³. Lastly, some claim Shareholder Theory precludes gifting corporate monies to charitable institutions or investing to raise employee morale. To the surprise of her enemies, Shareholder Theory rabidly supports those efforts, if and only if, this is the best use of capital to ultimately raise the dividend/growth rate en perpetuity.⁷⁴

⁷² Friedman, M. (2009). *Capitalism and freedom*. University of Chicago press.

⁷³ As a shareholder in the French industrial gases company Air Liquide, the dividend is increased by a maximum of 10%, granted to loyal shareholders for all direct shares held continuously for more than two calendar years. <http://www.airliquide.com/en/shareholders/the-stock-market-and-you/financial-glossary-1.html> Of significant note: French law provides with a general principal which states that "voting rights attached to capital or dividend shares shall be in proportion to the share of the capital they represent and each share shall entitle the holder Co at least one vote" (Article L225-122 of the French commercial Code). Consistent with the words "at least", the same French commercial Code (Article L225-123) enables companies to grant, subject to the satisfaction of certain requirements, double voting rights to their shares: "A voting right equivalent to twice that attributed to other shares may be attributed to fully paid shares which can be proved to have been registered in the name of the same shareholder for at least two years, depending on the proportion of the share capital they represent, by the memorandum and articles of association or a special shareholders' meeting."

⁷⁴ Bowie, N. E., & Freeman, R. E. (1992). Ethics and agency theory: An introduction.

Admittedly, Stakeholder Theory is at times also gravely misunderstood, most often when viewed as never demanding a company focus on profitability. Stakeholder Theory is most concerned that the corporation continues to exist en perpetuity since a bankrupt corporation creates value for no one, but all corporate gains must be attained by fairly weighing the interests of all stakeholders, including the shareholders. Since generally Stakeholder Theory provides no viable formula for mediating stakeholders' disparate interests, some claim the theory cannot be implemented. To their theoretical credit, Stakeholder Theorists have provided algorithms for trade-offs among stakeholders' interests. For example, one could assess risk each stakeholder took and rank them accordingly, or simply assert one specific stakeholder should always prevail, as recently argued by Richard Ellsworth.⁷⁵

Fiduciary law vests in shareholders: 1) the legal right to receive quality fiduciary services from management; and 2) the legal right to rely on the honesty of their managers by imposing on them not only a duty of loyalty, but other specific duties as well, to best prevent fiduciaries from swindling those entrusted interests. This aspect of fiduciary law is analogous to the tort of conversion and with the improper mens rea, the crime of embezzlement. A "fiduciary" relation thus, is a contractual one embodied by extremely high costs of specifying the how-to for management as well as the monitoring of that management. In lieu of detailed contractual terms, there is instead the duty of loyalty and if need be, the courts flesh out the duty of loyalty by delineating what the parties themselves would have wanted done if bargaining were cheap and all promises fully enforced.

Because agency problems arise from incomplete contracting, the duties of loyalty and care are standards empowering the court to complete the parties' contract as regards the facts and circumstances as they in fact unfolded. The duties of loyalty and care minimize transaction costs by drastically reducing the need for a contract clause to anticipate each and every future contingency. The contracting 1st parties need only address important contingencies that warrant the transaction costs of express provision, such as the possible subsequent inclusion of 3rd party beneficiaries. For all other contingencies, the fiduciary obligation fills the gap.

One can see the power of this when applied to a 3rd party beneficiary (stakeholder), thereby generally negating any further philosophizing as to a Stakeholder Theory when the legal contract principle of 3rd party beneficiary so readily inculcates it. Thus, Stakeholder Theorists can sleep at night, 3rd party beneficiary Contract Law is operating 24/7.

⁷⁵ Ellsworth, R. R. (2002). *Leading with purpose: The new corporate realities*. Stanford University Press. Ellsworth believes customers' interests should trump any other stakeholders.

Contract Law is most often quite sufficient to the task, having a rich body of interpretive authority on fiduciary matters across decades of case law, treatises, restatements, and evermore so, statutory codifications. This mass of knowledge lends a valuable predictability to guide corporate management on how the duties of loyalty and care will be applied to their situation. This guidance has already taken further specificity in the form of subsidiary or implementing rules on how to fully one's fiduciary duty. By now, fiduciary duties are endemic to both law and business, and are more akin to the invisible potency of oxygen; rather than, some moral crucifix each manager must carry while simultaneously rendering to Caesar his due: evermore profits.

Contra posed to the central tenets of Stakeholder Theory, fiduciary duties are not special duties from on high and are derived and enforced in the same way, as other contractual arrangements. Actual contracts always prevail over implied ones, which is why 3rd party beneficiary is needed since it makes "stakeholders" part of the contract. Without this, Stakeholder Theory is primarily moralizing, perhaps hoping that if such sermonizing prompts a majority in public opinion, a comprehensive statute will save the day. Yet despite decades of moralizing rhetoric about the inherent morality of fiduciary obligations, fiduciary duties in trust law are in today's world, unambiguously contractarian. Obviously in contract law, they are contractarian. In essence, much of the world and the value within it is nothing but a deal, hopefully fairly played out. This elan vital is neither Heaven on Earth, nor a dimension where the mere passage of Time increases Goodness. Best scenario is a Game refereed well, highly mindful of that which energizes so much of the Game⁷⁶. Yes, the Heart of Darkness.

C'est la vie!

⁷⁶ It is a highly volatile game involving Nature and gods of blood and bone. If corporate problems were just random mistakes, they could be predicted, contained and corrected. Man is not predictable, containable and incorrigibly Fallen.

COMPETITIVE INTELLIGENCE: AN EXPLORATORY LITERATURE REVIEW OF ITS POSITIONING

Alexander Maune *

Abstract

This article is a qualitative-exploratory literature review. The primary concern of the author is to explore the positioning of the competitive intelligence function within organisations so as to establish the best positioning. To ensure reliability of the literary exploration, only peer-reviewed journal articles were used. The findings of this article will make it possible to generalise about the best position of the competitive intelligence function and to develop some valuable propositions for future studies. The findings show that there is no single criterion on which to base the positioning of the competitive intelligence function within organisations. This article will assist business managers to understand and improve their positioning of the competitive intelligence function. This article has therefore academic value.

Key Words: Competitive Intelligence, Positioning, Exploratory Literature Review

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1. Introduction

As competition increases the world over, the demand for competitive intelligence (CI) is gaining popularity (Combs and Moorhead, 1993). Questions are, however, arising as to where organisations can best position the CI function.

There are many definitions of CI. According to McGonagle and Vella (2002), CI is defined as the use of public sources to develop data regarding competition, competitors and the market environment. CI then transforms, by analysis, such data into intelligence (McGonagle and Vella, 2002). They further state that public, in CI, means all information one can legally and ethically identify, locate and then access. CI is assumed to be both a process and a product in which information is transformed into actionable intelligence to be used as knowledge and foreknowledge when elaborating strategic products to inform decision-makers and to improve the quality of their decisions (Kahaner, 1996).

The position of CI within organisations is proving to be very critical now more than ever before (Kahaner, 1996). Kahaner (1996) further states that until recently, a common answer has been to place intelligence in strategic planning. Today, however, as the CI process finds application in companies beyond the strategic planning function, there is no single standard position for this capability (Miller, 2000). The position of CI functions is important because it often influences reporting relationships, budgets, and the type of projects undertaken. It is clear from the

studies that there is no single organisational structure used by the majority of organisations (Lackman, Saban and Lanasa, 2000). Gilad (2001) states that the debate on where best to position the CI function is an on-going one. He claims that many companies traditionally place the CI function under other functions and thereby limiting its scope to a narrow functional focus. Kahaner (1996) in support of this idea asserts that many organisations position the CI function in each business division such as marketing, sales, and research and development. Kahaner (1996), further claims that many large organisations place the CI function in strategic planning offices, which report directly to top management. This position, he asserts, makes the most sense if the CI function's main job is to support strategic planning, which is the case in most companies. There are many considerations for positioning the CI function.

Miller (2000) claims that there are a number of criteria to consider when deciding where to position the CI function. He states that factors such as a company's organisation, culture and market environment have a bearing in deciding where to position the CI function. The balance between strategic and operational intelligence requirements is also an important determinant (Miller, 2000). However, the ultimate determining criterion ought to be the locus of decision-making. Miller (2000) further claims that, for the CI function to have any effect on company performance, it should be positioned where it can provide direct support to both the strategic and day-to-day operational decision-making activities of an organisation. However, Miller's assertion is based

on the reasoning that, since the main task of CI is to support management decision-making, having a formalised CI system in place will go a long way in helping an organisation to address many different issues. To add to this debate, Kahaner (1996) claims that, since CI is not a function but a process, it should appear in all aspects of business as one seamless process not relegated to one area, division or unit.

According to Kahaner (1996), where CI is placed is not as important as how its lines of communication are configured. Kahaner (1996) asserts that, for maximum efficiency and power, CI should be placed high enough in the organisation that people will respect it and see that it has a senior champion. However, CI should be close to the prime users and must be accessible to everyone in the corporation (Kahaner, 1996, Salvetat and Laarraf, 2013).

As a research topic, CI has received much attention, especially in developed countries (Kahaner, 1997). Kahaner (1997) states that countries, such as France, Japan, Sweden and the USA, are more advanced compared to other countries, especially in Africa, in their embracement of CI as a means of enhancing competitiveness. However, there have been concerns on the positioning of the CI function within organisations by authors such as Kahaner (1997), Miller (2000) and Gilad (2001) who argue that unless the organisation of the CI function is done appropriately, its merits will not be fully recognised.

Very few academic works have tried to answer the following question: How is the CI function positioned within organisations? This article will help to establish the best possible position for the CI function within organisations through an exploratory literature review. Furthermore, some valuable propositions will be developed to generate questions and hypotheses that will help to guide further future research. Bless, Higson-Smith, and Sithole (2013) state that one must become more familiar with a phenomenon if one is to formulate more searching research questions or hypotheses. The remainder of this article presents the literature review, methodology, discussion of findings, and conclusion and recommendations.

2. Literature review

2.1 The competitive intelligence process

The CI process or cycle is usually divided by CI professionals into five basic phases, each linked to others by a feedback loop (McGonagle and Vella, 2012). These phases, making up what CI professionals call the CI cycle, are:

- Establishing the CI needs. This means both recognising the need for CI and defining what kind of CI the end-user needs (McGonagle and Vella, 2012).

- Collecting the raw data. First, a CI professional translates the end-user's needs into an action plan, either formally or informally. This usually involves identifying which questions need to be answered, and then where it is likely that he/she can collect the data needed to formulate the answers to these questions. From there, the collection begins, both of secondary and primary data (McGonagle and Vella, 2012).
- Evaluating and analysing the raw data. During this phase, the data that was collected is evaluated and analysed, and is transformed into useful CI. That may be done by the person doing the collection or by a separate CI analyst. If one fails to use some analysis during the collection process, one might waste hours collecting useless information (McGonagle and Vella, 2012).
- Communicating the finished intelligence. This involves preparing and presenting the results in a usable format and in a timely manner. The CI may have to be distributed to those who asked for it and, in some cases, to others who might also benefit by having it. Timeliness and security of the finished intelligence are all important aspects to consider before communication (McGonagle and Vella, 2012).
- Taking action. This means the end-user actually uses the CI in decision-making. The CI may be used as an input to decision-making, or it may be the first of several steps in an overall assessment of, for example, a new market. The decision of how and when the CI is used, is made by the end-user and not by the analyst (McGonagle and Vella, 2012).

2.2 The importance of competitive intelligence

According to the findings of McKinsey study (McKinsey, 2008) that asked executives how their firms responded to a significant price change by a competitor or to a significant innovation by a competitor, the majority of executives in both groups, across regions and industries, said their companies found out about the significant competitive move too late to respond. CI is considered valuable, even though virtually all evidence of the value and effect of the process are to date anecdotal or deals with indirect assessments (McGonagle and Vella, 2002). In the early 1990s, a study of the packaged food, telecommunications and pharmaceutical industries reported that organisations that engaged in high levels of CI activity show 37% higher levels of product quality, which in turn could be associated with a 68% increase in business performance (Jaworski and Wee, 1993). In the mid-1990s, NutraSweet's chief executive officer (CEO) valued its CI at USD50 million. This figure was based on a combination of revenues gained and revenues which were "not lost"

to competitive activity (Flynn, 1994). A more recent PricewaterhouseCoopers' study (PricewaterhouseCoopers, 2002) of CEOs reported that virtually all CEOs surveyed (84%) view competitor information as important to profit growth of their company.

2.3 The main competitive intelligence players

The CEO inspires in his subordinates/employees a will to practice some form of CI by transmitting to the employees some knowledge and know-how, and in this way, get all the employees to become part of a CI culture (Salvetat and Laarraf, 2013). These two authors also claim that the other role of the CEO is to provide training of financial and social incentives. The CEO always leads the CI function within an organisation. Managerial policies must create awareness and legitimise the CI process with human resources for company policy formulation. The number of employees dedicated to a CI function should be in proportion to the size of the organisation (Lackman et al., 2000). Lenz and Engledow (1986) state that the number of employees dedicated to a CI function should be between one to seven employees, whilst Prescott (1999) confirms that there should be three full-time staff, one part-time secretary and a monitoring team. Salvetat and Laarraf (2013) state that the majority of these employees that are involved in the CI process are not information experts and therefore they do not participate as full-time employees. They further claim that it is the most seasoned and former staff, in the CI subject, who occupy the position of manager. Information experts are therefore full-time employees in CI practices. CI key players within organisations are at times difficult to identify (Salvetat and Laarraf, 2013). According to the study by Salvetat and Laarraf (2013), based on 1500 firms in the European Union, the involvement of managers in the CI process is strong although the awareness of this practice among employees remains low. The results of the study by Salvetat and Laarraf (2013) show that on one hand an organisation which structures its CI unit weakly does not employ experts and on the other hand, an organisation which structures its CI unit strongly employs many experts. More so, it appears that the presence of information experts within an organisation will allow the building of a structured and independent CI unit (Salvetat and Laarraf, 2013).

2.4 Determining factors for positioning the competitive intelligence function

Until recently, little thought had been given to the question of where in a corporate organisation to place the CI process/function (Sawka, 2001). Strategic planning or other functions akin to it, for the most part has been the most logical fall-back location

(Sawka, 2001). CI units were concerned mainly with issues of strategic importance to a company, and the strategic planning department seemed to be the most logical choice for placing the CI function. Miller (2000) states that, as more and more U.S. companies have embraced the concept of CI and have set on the path of developing and managing robust CI functions, strategic planning is no longer the important reaction to the question of where to locate the CI unit. He further states that indeed, more and more companies are electing to place their intelligence programme within sales and marketing, finance, operations, and other corporate functions. Miller (2000) adds three forces that seem to be behind the expansion of reasonable locations for company CI functions.

CI functions, like any other organisational functions, have many needs that must be met for the CI process to pay dividends that are measurable to the organisation (Sawka, 2001). CI functions must be located where they can support decision-making by providing intelligent information, discussing alternatives and compelling action. It is argued that whether CI units address strategic or tactical needs is almost irrelevant; CI must be as close to the decision-maker as possible.

One mistake many companies make is to locate the CI function in such a way that layers of bureaucracy exists between them and the decision-makers they are ultimately intended to serve. Whether decision-makers are senior corporate staff or district sales managers there should be no filters between them and the CI staff (Miller, 2000).

CI functions should be highly visible in organisations. Miller (2000) states that, unlike the government or military, where CI activity is necessarily shrouded in secrecy, corporate CI functions should not take steps to mask their day-to-day activities. CI units should have strong links to other parts of the organisation. In many cases, this requires indirect relationships with other staff and departments in addition to the direct reporting lines the CI function already has.

CI functions must be located in places where they will be adequately nurtured. Companies usually fail to support the CI process. Miller (2000) states that too often executives speak of the need for a robust intelligence process and then designate an already overworked market research analyst to serve as the company's CI person. Furthermore, Miller (2000) states that CI functions that should have any significant influence on corporate decision-making and competitiveness must exist (must be placed) within a section of the organisation where it can be well staffed and have technological and other support. Organisations must be able to provide adequate staff, technology and other support.

Though strategic issues, such as long-term planning, capital investments and technological matters still tend to play an important role, companies no longer adopt and apply intelligence systems to

meet purely strategic needs. The greatest challenge is to strike the right balance between strategic and tactical needs to avoid an imbalance (Miller, 2000). Miller further argues that other industries, too, are finding that CI departments are well suited to address highly operational matters.

Decentralisation of the organisational structure in many firms is opening up new opportunities for a variety of organisational functions to house the CI system “empowerment”, and the pushing of decision-making downward to operational levels has made CI more applicable at a number of levels within an organisation. Many companies are creating virtual networks of CI professionals within their organisations, linked together through formal and informal mechanisms.

Perhaps most important, the locus of priority on CI issues is – rightfully – having a greater impact on

the decision of where to locate the CI process (Miller, 2000). It has been recognised that CI systems succeed only when they are demand-driven, that is, when they are organised to provide insight and clarity to competitive issues that decision-makers have identified as important to a company’s competitive success (Miller, 2000). Miller (2000) further states that CI systems are increasingly being developed to address specific competitively important issues, and being placed in organisational structures where those issues tend to have the greatest effect.

The combination of the determining factors and organisational options depicted in Figure 1 below provides a framework that companies can use to help guide their decision as to where to locate the CI unit, (Miller, 2000) but it is by no means applicable to every situation.

Figure 1. Locating the intelligence unit: An organisational framework

	Strategic vs. tactical	Corporate organisational structure	Locus of decision-making
Centralised	Weigh toward strategic focus	Strong corporate staff	Little empowerment
Decentralised	Weigh toward tactical focus	Highly autonomous strategic business units	Complete empowerment
Hybrid	Mix of strategic and tactical needs	Balance of power among corporate and divisional staffs	Consensual decision-making.

3. Methodology

This article is qualitative in nature and a literature review was conducted on some of the identified peer-reviewed and published journal articles on CI and its positioning or structuring. To identify relevant literature/journals, academic databases and search engines were used. A review of references in related studies led to more relevant sources, the references of which were further reviewed and analysed. Keywords such as, ‘competitive intelligence’, ‘structuring’, and ‘positioning’ were used in search engines to find relevant sources. To ensure reliability, only peer-reviewed articles were used. The researcher skimmed through the text of the journal articles first, checking whether it was relevant for the purpose of this research article. Reviewing data of existing journal articles was necessary to enhance the generalisability of the findings (Morse, 1999). The purpose of this review was to identify the contributions of research in advancing the understanding of the CI function’s positioning in organisations.

Criteria for inclusion of articles in the review included the following:

- Written in English
- Published in peer-reviewed journals
- Cited CI structuring or positioning

4. Structuring the competitive intelligence function within organisations

Companies’ efforts to weigh the determining factors of strategic versus tactical needs, decentralised organisational structures, and the locus of decision-making lead to the availability of general organisational structures for the CI function. The organisational options most companies typically face are highly centralised systems that report to a single corporate entity, decentralised systems that typically incorporate multiple CI units serving several organisational components, or hybrid systems that combine features of both previous options (Miller, 2000, Du Toit and Muller, 2004). Salvetat and Laarraf (2013), however, add in-sourcing or out-sourcing and formalisation or non-formalisation as other organisational options available for adoption. Providing precise of CI systems becomes therefore difficult since particular company CI requirements differ from company to company. As a result, Miller (2000) argues that CI systems must be highly customised for each individual company choosing one to pursue. Lackman et al. (2000) carried out a study on 16 companies.

According to a benchmarking study of 16 companies that was conducted by Lackman et al. (2000) to determine how the market intelligence function was structured in these enterprises, it was

found that there was no single organisational structure which was used by the majority of firms. It was found that the CI function was in the marketing/marketing research (46%) or sales (14%) departments. At most companies, the CI function relied on internal sources. The study by Lackman et al. (2000) also found that two thirds of the enterprises sourced their intelligence from outside, fewer than six times per year. It was also found that those organisations with a more established CI function had senior management playing a critical role (67%) in the assessment of intelligence needs than those organisations with a less established CI function. Usually, the CI function is organised within the marketing or market research departments (Michaeli, 2004).

4.1 Centralisation of the competitive intelligence function

Centralised CI functions start with the premise that strategic needs dominate, and that decisions regarding strategy (planning and execution) are made by corporate decision-makers (Miller, 2000). As a result, these systems tend to stand alone, relying on informational and analytical inputs from throughout the organisation. Miller (2000) states that these centralised CI functions report most commonly to a senior corporate officer who is responsible for not only providing the necessary organisational support for the CI process – in terms of budgets, personnel and other resources – but also for leading the effort to define and refine intelligence requirements among executive management. In a highly centralised organisational structure, top executives retain authority for most strategic and operating decisions and keep a tight rein on business unit heads and department heads; comparatively little discretionary authority is granted to subordinate managers (Sawka, 2001). The intelligence delivered is highly analytical, forward looking, and typically has a longer shelf life than intelligence provided by decentralised systems serving more tactical needs. Centralised CI practices are mostly observed in large firms (Levet, 2002 in Salvétat and Laarraf (2013), Bournois & Romani, 2000, Salles, 2006). According to the GIA's survey (GIA, 2005), it was found that in larger companies in particular, the CI function was performed in-house within a centralised unit but that certain areas of the CI function might be out-sourced. The GIA's survey (GIA, 2005) also found that there was no right or wrong concerning centralising the CI function. The findings of the study also show that in some countries such as Finland, companies have an equal number of centralised and decentralised units, while in Mexico, companies are inclined towards centralised units.

According to Levet (2002) in Salvétat and Laarraf (2013), thanks to his study based on eight French small to medium enterprises (SMEs), 39% of firms practice a form of CI without a monitoring department. CI function is often centralised at the top

management levels in SMEs, while it is rather decentralised with information experts in large firms (Pearce, 1982). Salvétat and Laarraf (2013) assert that the centralisation of the CI process provides a global vision, a rapid satisfaction of information needs, facilitates analysis, reduces duplication and ensures motivated and trained employees. The centralisation of the CI process is preferred (Porter, 1985) for acquiring legitimacy for the CI approach with employees. According to the findings by Lackman et al. (2000), the CI process is centralised in 46% of firms, especially at the top management level (55%). A centralised system reduces redundancy and makes it easier for the data to be assembled and shared, since all divisions transmit their information to a single, organised unit. This procedure, according to Greene (1988), enhances the coordination and sharing of data. Centralisation assumes that information can be processed and transferred from one point to another without much difficulty (Pirttila, 1998). Johnson (2005), however, states that centralised, command-and-control CI practices have been called into question by the very theories driving modern decision science.

4.2 Decentralisation of the competitive intelligence function

Stubbart (1982) is in favour of a decentralised CI practice within each functional section of an organisation. Indeed, the decentralisation of the CI function/process allows multi-actor and multi-domain expertise, information better targeted to needs, and a monitoring activity more operational and better integrated with the decision-making process. Digital technology has enabled more and more organisations to adopt decentralised systems (Miller, 2000). Decentralised CI functions consist of multiple intelligence employees who are proliferated throughout the organisation. Decentralised CI functions provide tactical intelligence requirements and rarely provide these to senior management. Miller (2000) further states that these decentralised CI functions may or may not be accompanied by separate, smaller organisational employees. Two problems, however, arise from this type. There is the redundancy or duplication of effort, as each department strives to collect the information it needs. CI also depends on the convergence of data to function properly and, with a decentralised system, that confluence is much more difficult to achieve (Greene, 1988). On the other hand, the advantage of a decentralised unit is its dependence on interpersonal networking that leads to information sharing and spontaneous team building (Hall, 2000).

4.3 Hybrid competitive intelligence function

Hybrid CI functions combine attributes of both centralised and decentralised functions (Du Toit and Muller, 2004). Salvetat and Laarraff (2013), in support of Du Toit and Muller (2004), state that there is a mix of centralisation and decentralisation regarding CI practices. They further found that CI practices are focused on the top managers and information experts, but decentralised to middle managers. Salvetat and Laarraff (2013) supports Terry (1977), who recommends that firms must have both centralised and decentralised CI units. Miller (2000) states that multiple CI units may exist throughout each organisation, but they are usually fewer in number as compared to single CI units. The CI needs of senior executive members are the overriding driving force in setting intelligence targets and requirements, though hybrid systems usually have the flexibility to be able to address ad hoc operational needs as well. CI methodologies for the collection and analysis of information are fairly consistent throughout the organisation, and the number and type of intelligence products are equally uniform (Miller, 2000).

4.4 In-sourcing or out-sourcing of the competitive intelligence function

The problems of internally managed and executed CI models have given rise to out-sourced models, that is, the out-sourced CI project model or the complete third-party model (Eaton, 2003). Out-sourcing is typically considered when cost-cutting is taking place but also when the necessary support from top management is lacking. Having high-level management on board is critical to a successful CI function (Miller, 2000, Fleisher & Bensoussan, 2002). Muller (2009) states that obtaining an external view and assistance will be beneficial as this brings new objective ideas. Out-sourcing is also considered in cases where the CI function is performed as an additional function. Muller (2009) claims that, with regard to the use of resources, time and expertise, out-sourcing will be beneficial. A benefit of out-sourcing to a supplier that specialises in real CI is the provision of a forward-looking analysis and opportunity analyses that go far beyond simple librarian-style information. Out-sourcing is also considered in cases where certain information is unavailable or difficult to access from an internal CI function's point of view, or when companies might feel uncomfortable to gather certain information, or when key external expertise is required (Muller, 2009). The best legally attainable intelligence is available within a company and from a company's customers, suppliers and people in the field, including sales people and marketing people and merchandisers. However, often CI personnel are discouraged to talk to such external sources and, if they were permitted to do so, it would

be difficult to obtain honest views (Muller, 2009). CI ensures that the sales force is integrated in the corporate intelligence network (Galvin 2001). Out-sourcing CI presents no barrier to the ethical collection of data from external experts (Eaton, 2003).

Eaton (2003) and Johnson (2005) state that there are advantages and disadvantages to the out-sourcing model. The advantages include an enhanced external objectivity and a professional stature within the client, unattainable by lower-level internal employees, access to specialist processes, skills and tools and openness to contact customers, suppliers and other professionals who are often shielded from interaction with internal staff. Out-sourcing also helps create a larger strategic context into which the competitive data is placed. Most CI focuses upon the threats to the company represented by specific competitive activity but, often, a threat could also give rise to an opportunity for the company. Such opportunities are often neglected. The out-sourced CI professional might be bolder in providing alternative outcomes to a competitive situation than a person from within the organisation. This added analysis of the implications of the data could be a valuable resource.

Experts argue that perhaps the most significant advantage of out-sourcing is the building of a longer-term CI capability (Malhotra, 1996, Eaton, 2003). Having a long-term relationship with an external third-party consulting company means that resources are available to build a larger awareness capability throughout the client company. Companies that may consider out-sourcing CI should be aware of the potential problems that exist when out-sourcing CI or when considering an external third-party project-oriented CI capability. CI vendors may lack the unique company view and knowledge on an industry (Muller, 2009). According to Muller (2009), CI vendors are also not given the necessary access to place a given specific CI issue within the broader strategic context of the client's organisation. Furthermore, out-sourced projects are often short-term focused interventions, resulting in the client company being left without significant new skills, knowledge and CI aptitude.

A CI vendor would typically focus only on the narrow issues described within the scope of the project agreed upon, perform the study, and deliver the results and leave (Eaton, 2003). The failure to install a process that puts the immediate competitive threat within its broader strategic context or leave behind an empowered organisation makes the out-sourced CI project approach inefficient. Out-sourcing can also be costly and often does not provide the expected return on investment due to its limited capacity.

The CI function concerns information management (Salvetat and Laarraff, 2013). For this reason, Salvetat and Laarraff (2013) argue that CI

should remain largely in-sourced. However, there is still division on the necessity of in-sourcing. Even though information is strategic for an organisation as stated above, there are other activities of the CI process that are out-sourced to specialised service providers. The use of service providers is a complement to existing internal CI activity. A number of models are emerging related to the out-sourcing of key CI functions (Eaton, 2003). Fahey and King (1977), recommend an internal and autonomous CI function, based on a study of 12 American organisations. According to studies by Jain (1984) and Prescott (1999), 30% of firms have an internal CI department.

Out-sourcing pieces of the value chain formerly performed in-house makes strategic sense whenever:

- An activity can be performed better or more cheaply by outside specialists. An outsider, by concentrating specialists and technology in its area of expertise, can sometimes perform these services better and more cheaply than a company that performs the activities only for itself (Quinn, 1992).
- The activity is not crucial to the firm's ability to achieve sustainable competitive advantage and would not hollow out its core competencies, essential skills or technical know-how (Quinn, 1992). Critics agree about the fact that extensive out-sourcing can hollow out a company, leaving it at the mercy of outside suppliers and barren of the skills and organisational capabilities needed to be master of its own destiny (Chandler, 1962).
- Out-sourcing reduces the company's risk exposure to changing technology and/or changing buyer preferences.
- Out-sourcing streamlines the operations of the company in ways that improve organisational flexibility, cut cycle time, speed up decision-making, and reduce coordination costs.
- Out-sourcing allows a company to concentrate on its core business and to do what it does best.

4.5 Formalisation or non-formalisation of the competitive intelligence function

Within firms, information is correlated with the level of progress of monitoring activities (Salvetat and Laarraf, 2013). A study by Phanel and Levy (2002) based on 75 French SMEs, shows that 17.5% formalised CI procedures were used for the collection of information, 22.5% for its analysis, and 50.5% for its dissemination. Peters and Waterman (1982) show that 72% of managers want a formalised CI function/process whilst the rest were of the other opinion. A study by Bournois and Romani (2000, in Salvétat and Laarraf, 2013) based on 5000 European firms, showed that only 12.4% of firms have a formalised CI function/process, whereas Dissenbach

(1983) maintains that 73% of firms have a formalised process. Gilad and Gilad (1985), however, state that the formalisation of the CI process allows for better quality, quantity, targeting, efficiency and reliability of information. However, non-formalisation reduces organisational, operational and training costs. Salvétat and Laarraf (2013) argue that, although formalisation is seen as generally good, strong formalisation can be seen as a tool to control employees and as a lack of creativity because of its standardisation, thus limiting a competitive advantage.

5. Conclusion and recommendations

The primary concern of the author of this article was to explore how the CI process is positioned in organisations and to establish the best positioning. The research found that the single most important criteria, according to Miller (2000), on which to base the position of the CI function within the organisation is the location of those decision-makers who have an expressed need for CI and who are willing to provide requirements-based targets. In addition, it is possible for several decision-makers or decision-making components to be served by a single CI function, as long as the needs are roughly comparable and are not divided among strategic and tactical issues. The research found that there is no hard and fast rule for CI positioning. The following guidelines, adopted from Miller (2000), are worth recommending. Several CI functions are likely when an organisation has strong needs for both strategic and tactical CI; thus it becomes impossible for one CI staff to meet both requirements.

It is recommended that whatever CI structure an organisation decides upon, it requires flexibility to support decision-making at all levels continuously. Miller (2000) argues that it is rare for CI programmes to maintain a single organisational structure and remain in one corporate position forever. More so, CI needs to be flexible and adaptive to shifting market needs and strategic requirements. It is also recommended that CI functions be structured to maintain a balance between strategic and tactical needs. Miller (2000) argues that tactical needs are as important as strategic needs and that it is a mistake to think that strategic needs are more important than tactical needs.

The people involved in the CI function must recognise the importance of process coordination at all levels. Mechanisms to ensure coordinated processes become very important as many companies set up several CI units. Miller (2000) states that inefficiencies are sure to exist if CI staff members are left to develop their own procedures independently of one another. Duplication of effort, internal miscommunications and incompatible CI products are only a few of the missteps an organisation is likely to experience if it fails to coordinate its CI activities. Miller (2000) further states that, as a rule of thumb,

the greater the number of separate CI functions a company has, the greater the number of resources it will need to bring to bear to ensure consistency of operations among them.

Given all the arguments by different authors and from different researches, one can conclude that there is no one-size-fit-all when it comes to the position of the CI function within organisations. The position of the CI function is situational, that is, it differs from one organisation to another and there are factors that go by each position such as culture, market environment and the company's organisation which differs from one organisation to another. The best position of the CI function is where it can provide direct support to decision-making although there seems to be a shift away from purely internal CI function towards out-sourcing of the CI function.

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DESCRIPTIVE BUSINESS INTELLIGENCE ANALYSIS: CUTTING EDGE STRATEGIC ASSET FOR SMES, IS IT REALLY WORTH IT?

*Sivave Mashingaidze **

Abstract

The purpose of this article is to provide a framework for understanding and adoption of Business Intelligence by (SMEs) within the Zimbabwean economy. The article explores every facet of Business Intelligence, including internal and external BI as cutting edge strategic asset. A descriptive research methodology has been adopted. The article revealed some BI critical success factors for better BI implementation. Findings revealed that organizations which have the greatest success with BI travel an evolutionary path, starting with basic data and analytical tools and transitioning to increasingly more sophisticated capabilities until BI becomes an intrinsic part of their business culture and ROI is realized. Findings are useful for managers, policy makers, business analysts, and IT specialists in dealing with planning and implementation of BI systems in SMEs.

Key Words: Cutting Edge, Business Intelligence, Asset, Strategic

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1. Introduction

Leading organizations of all kinds are seeking new, smarter ways to improve performance, grow revenue, develop stronger customer relationships and increase workforce effectiveness – and they expect individuals in every role to contribute to these outcomes (Negash, 2004). Business intelligence (BI) is the only key factor in achieving such results because it supports informed decision making at every level, enabling managers, executives and knowledge workers to take the most effective action in a given situation (Chen, Chiang, & Storey, 2012). Business intelligence (BI) software connects people with information when and where they need it, and provides capabilities far beyond spreadsheets to deliver a true picture of the business. The SME e-Access and Usage survey which was carried out by the Research ICT Africa (RIA) Network in 14 African countries between the last quarter of 2005 and the first quarter of 2006 revealed ICT is the best vehicle for information systems management (Unwin, 2005). Its primary objective is to understand the impact of ICTs on private sector development, and how ICTs can contribute to a vibrant SME sector and economic growth in the context of developing economies (Unwin, 2005). The countries covered included Botswana, Cameroon, Ethiopia, Ghana, Kenya, Mozambique, Namibia, Nigeria, Rwanda, South Africa, Tanzania, Uganda, Zambia and Zimbabwe. SMEs account for the employment of at least 57% of

the productive population in Zimbabwe and the entire sub-Saharan Africa. The current formal unemployment rate in Zimbabwe is approximately 80% (Robertson, Smith, and Tunzelmann, 2009). This figure is fast increasing due to the shrinkage in the formal sector, subsequent retrenchments and the outpouring of graduates from tertiary institutions joining employment seekers while the formal sector can only absorb 20 000 graduates or less annually (Ndlovu & Ngwenya, 2003).

Robertson et al (2009) stipulates that with 80 percent formal unemployment and shrinking productivity, few of the 2 million young people and graduates who turned 18 years, since 2000 found jobs with a regular income, training, advancement or career prospects in SMEs. Small and medium-sized enterprises (SMEs) are the life blood of global economy. Nearly ninety-five (95) per cent of the enterprises in most economies belong to the group SME (Ebrahim, Ahmed, & Taha, 2010). In Zimbabwe, an MSME Policy and Strategy Framework has defined small and medium enterprises as those who are registered in terms of their legal status' and 'employing anywhere between six to <100 workers' (Zimbabwe, 2008: 20). The official definition of SMEs in Zimbabwe includes heterogeneous, formal enterprises and informal businesses which are complemented by estimates of the size of the informal economy. Just like the rest of the world, number of employees, total assets, sales and investment levels are commonly used yard-sticks.

Various activities of SMEs include village handicraft makers, restaurants, computer software, shops, and many sophisticated skills that drive different markets. Zimbabwe defines SMEs according to a lower limit of 5-10 employees and an upper limit of 50-100 employees for a small organisation. Medium enterprises were defined to have lower and upper limits of 100 and 250 employees (Ndlovu & Ngwenya, 2003). The EU describes an SME as a company that has fewer than 250 employees and has either an annual turnover not exceeding €50 million or an annual balance sheet total not exceeding €43 million (Perrini, 2006). But (Olawale, & Garwe, 2010) stipulates that one of the primary causes of failure in these small enterprises is lack of information systems (business intelligence) that is the ability of an organization to collect, maintain, and organize knowledge wishing to stay in business they have to compete in a different way (Negash, 2004). Innovativeness and competitiveness of SMEs can be increased by means of information technology implementation. Enterprise that made use of information technology oriented investments obtained substantial profits (Negash, 2004).

Unfortunately, information technology related solutions are mainly oriented in large enterprises and corporations but not in SMEs. Putting the latest information technology related solutions into practice of SMEs is frequently much delayed in comparison with large enterprises or does not happen at all (Olawale, & Garwe, 2010). As a result, SMEs are not as competitive in the market as large enterprises and their development is questionable. Business Intelligence (BI) as a concept provides a means to obtain crucial information to improve strategic decisions and therefore plays an important role in current decision support systems in SMEs (Baars, & Kemper, 2008) and is about creating value for organizations based on data or, more precisely, facts. Business intelligence enhances decision-making capabilities for managerial processes for instance planning, budgeting, controlling, assessing, measuring, and monitoring and to ensure critical information is exploited in a timely manner (Baars, & Kemper, 2008). According to Baars, & Kemper, (2008), the data warehouse industry – as the technological basis of BI – has reached full maturity and acceptance in the business fraternity. The pursuit of improving financial results, as well as production capacity or sales figures, results in several (ad-hoc) decisions, impacting the operational, tactical and strategic levels hence the need for business intelligence systems. Bierly, Kessler, & Christensen (2000) defined knowledge as a clear understanding of information; transformation from data (raw facts) to information (meaningful, useful data) is specified as the process of gaining knowledge. Usage of gained or extracted knowledge to establish and achieve goals, set by an organization, is described as wisdom or business intelligence.

The ability to import data seamlessly from as many sources as possible and to offer an integrated view over them without the need to define a-priori schemas offers flexibility and removes barriers in terms of what analyses are possible and what they can reveal (Westerski, 2013).

Given the dearth of literature on Business Intelligence in Zimbabwean SMEs this article saves a documentary overview of Business Intelligence as a cutting edge strategic asset. It is against this backdrop that the article seeks to discover whether it is worthwhile having business intelligence systems adopted by SMEs in Zimbabwe. The main purpose of this article is to capture the essence of what the literature says about BI and its role in decision-making in SMEs in general and in particular, to find out the expectations and empirical observations of the use of the BI output in decision-making in SMEs, to explore every facet of Business Intelligence, including internal and external BI and the tangible/intangible aspects leading to a competitive advantage in SMEs.

Internal Business Intelligence (BI) refers to the protection and utilization of internal data and external BI refers to the gathering of data and information about the competition (Wright, 1999). External Business Intelligence involves a company's attempts to gain information about a competitor to gain an advantage. Many researchers have identified numerous barriers/inhibitors confronting small and medium enterprises (SMEs) in their quest to adopt and assimilate electronic (e)-commerce applications in their operations (see for example, (MacGregor, & Vrazalic, 2005) and prescribed a plethora of solutions to make SMEs competitive.

To the best of my knowledge no research has been done in this area, "Descriptive Business Intelligence Analysis: Cutting Edge Strategic Asset in SMEs in Zimbabwe". A documentary analysis review of some of the most cited pieces of peer reviewed articles on this topic will be unraveled to see how BI has contributed to organizational growth in countries outside Zimbabwe, and again how it has cut costs in those companies. The reason is to find whether it is worth applying in Zimbabwean economy. The findings are then used to recommend stakeholders of SMEs in Zimbabwe to adopt the Business Intelligence strategy. In view of this background, the article is to contribute to literature on business intelligence espousal and utilization by SMEs, predominantly giving an answer to the question: "Is business intelligence really worth it as cutting edge strategic asset in Zimbabwean SMEs?". The answer will be arrived at by conducting a descriptive documentary analysis of text around the topic. The findings will contribute to the sea of knowledge as no such research has been done in Zimbabwe and again the results obtained may be useful for managers, policy makers, business analysts, and IT specialists in

dealing with planning and implementation of BI systems in SMEs.

2. Descriptive Research Methodology: Documentary Analysis

For the purpose of this article a descriptive research methodology has been adopted, because it is restricted to factual registration and that there is no quest for an explanation why reality is showing itself this way (Tsang, 1997). In principle, descriptive research is not aiming at forming hypotheses or development of a theory (Creswell, 2002). Through document analysis, descriptive research is about describing how reality is in the business ecosystem. With descriptive research in its purest form explaining and evaluating is left to the reader or to other disciplines (Krathwohl, 1993). Document analysis is the systematic exploration of literature from various disciplines, IT, business, entrepreneurship psychology, or other artefacts such as films, videos and photographs. Hanson et al., (2005) argued that documents are unobtrusive and can be used without imposing on participants; they can be checked and re-checked for reliability. This methodology emphasizes an integrated view of speech/texts and their specific contexts. Texts in documentary analysis can be defined broadly as books, book chapters, essays, interviews, discussions, newspaper headlines and articles, historical documents, speeches, conversations, advertising, theater, informal conversation, or really any occurrence of communicative language (Robson, 2002).

Two criteria pivoted the selection criteria of literature that serves as the bedrock for this article. First, the selected literature for review needed to explicitly describe or explain the business intelligence inaccessible terms and also the literature from the texts needed to be general and all encompassing. General texts according to Robson (2002) are respected journals and sections of journals focusing on these disciplines for entrepreneurship, IT and business intelligence served as secondary sources for this article. Keywords such as intelligence, business, SMEs, cutting edge, were used to query databases such as Web of information systems, JSTOR (a digital library founded in 1995 and originally containing digitized back issues of academic journals, and it now includes books and primary sources, and current issues of journals), and UNISA Electronic Databases such as Sage Journal, EBSCO, SABINET

3. Literature Review on Business Intelligence

3.1 The Evolution of Business Intelligence

Business intelligence is not just a modern idea. In his famous treatise "The Art of War, Sun Tzu says,

"...what enables the wise commander to strike and conquer, and achieve things beyond the reach of ordinary men, is foreknowledge (Parry-Giles, & Parry-Giles, 1999). Now this foreknowledge cannot be elicited from spirits..." (Parry-Giles, & Parry-Giles, 1999). Although the term 'business intelligence' has been in use since 1800, (Lin, Michel, Aiden, Orwant, Brockman, & Petrov, 2012), it was used in scientific context for the first time in an article by Hans Peter Luhn, an IBM researcher, in 1958 (Gibson, Arnott, Jagielska, & Melbourne, 2004). In his article, Luhn (1958) described an "automatic method to provide current awareness services to scientists and engineers" (p. 314) who needed help to cope with the growth of scientific and technical literature (Gibson, et al, 2004). While Sun Tzu is not the father of business intelligence, his concept that foreknowledge breeds success applies directly to BI. Modern BI uses computers to gain foreknowledge by processing and analyzing information in support of business decisions. In the 1980's before BI was BI it was called Executive Information Systems (EIS), in the 1990's, it was Online Application Protocol (OLAP), followed by scorecards, dashboards, KPIs (key performance indicators), and real time alerts through business activity monitoring (Gibson, et al, 2004).

The term BI was coined by Gartner (Dresner, 1989) as an umbrella term to describe the set of concepts and methods used to improve business decision-making by using fact-based support systems. In the 1990s, information technologies (IT) evolved to enable resource wide applications such as Customer Relationship Management (CRM), Enterprise Resource Programs (ERP) and Supply Chain Management (SCM) that help streamline many large and medium sized businesses to make them competitive (Dresner, 1989). In addition, in the late 1990s, IT enabled the process of data warehousing, especially for transaction-intensive industries such as financial, retail and telecommunications (Kotrlik, & Williams, 2003). As a result, there are vast amounts of information stored in company computers about all aspects of the business. Regardless of the moniker we give BI, it is certain that it is here to stay. Research on business intelligence originates from the term as introduced in 1989, by Howard Dressner, regarding business intelligence to describe concepts and methods to improve business decision making by using fact-based support (Negash & Grey, 2008).

From a historical standpoint the underlying concept of business intelligence is not new. Since ancient times, humanity has developed processes, techniques and tools for collecting and analyzing intelligence to support decision making, especially during times of war (Rutkauskas, 2008). Ancient military organizations developed tactics and methods to collect and develop intelligence although these were more in terms of what we today call "industrial espionage", that is illegal and unethical methods to

collect intelligence about other organizations (Calof and Wright 2008).

3.2 Business Intelligence: Definitions & Approaches

The BI literature lacks a universally accepted definition of BI (Ponelis, & Britz, 2013). The definitions range from one-dimensional definitions, in which BI is viewed as a set of technologies or as a process, to multidimensional definitions, in which BI is viewed as a process, a set of technologies and a product (a detailed discussion about the BI definitions is provided in chapter two). In line with the multidimensional view, Davenport (2006) defines BI as a term which encompasses a wide array of processes and software to collect, analyze, and disseminate data, all in the interest of better decision-making." In the same way, Wixom and Watson (2010) define BI in their paper as: "a broad category of technologies, applications, and processes for gathering, storing, accessing, and analyzing data to help its users to make better decisions." A literature review around the theme business intelligence (BI) shows "division" in endeavor to define this concept or division in attempts at defining this concept: Technical and managerial approaches, tracing two broad patterns: The managerial approach sees BI as a process in which data gathered from inside and outside the company are integrated in order to generate information relevant to the decision-making process. The role of BI here is to create an informational environment in which operational data gathered from transactional systems and external sources can be analyzed, in order to reveal "strategic" business dimensions. The BI literature lacks a universally accepted definition of BI (Ponelis, & Britz, 2013). The definitions range from one-dimensional definitions, in which BI is viewed as a set of technologies or as a process, to multidimensional definitions, in which BI is viewed as a process, a set of technologies and a product (a detailed discussion about the BI definitions is provided in chapter two). In line with the multidimensional view, Davenport (2006) defines BI as a term which encompasses a wide array of processes and software to collect, analyze, and disseminate data, all in the interest of better decision-making. According to Hannula et al, it is the Systematic business information acquisition and analysis.

In addition, it is also called Competitive Intelligence, Corporate Intelligence, Market Intelligence, Market Research, Data Warehousing, and Knowledge Management. Howard Dresner (1989) proposed "business intelligence" as an umbrella term to describe "concepts and methods to improve business decision making by using fact-based computerized support systems." It was not until the late 1990s that this usage was widespread.

Ranjan, (2009) defined Business intelligence as the process of taking large amounts of data, analyzing that data, and presenting a high-level set of reports that condense the essence of that data into the basis of business actions, enabling management to make fundamental daily business decisions. Ranjan, (2009) view BI as way and method of improving business performance by providing powerful assists for executive decision maker to enable them to have actionable information at hand. BI tools are seen as technology that enables the efficiency of business operation by providing an increased value to the enterprise information and hence the way this information is utilized. Wang, Carley, Zeng, & Mao, (2007) define BI as "The process of collection, treatment and diffusion of information that has an objective, the reduction of uncertainty in the making of all strategic decisions." Experts describe Business intelligence as a "business management term used to describe applications and technologies which are used to gather, provide access to analyze data and information about an enterprise, in order to help them make better informed business decisions." Tvrdikova (2007) describes the basic characteristic for BI tool is that it is ability to collect data from heterogeneous source, to possess advance analytical methods, and the ability to support multi user's demands. Zeng et al. (2007) categorized BI technology based on the method of information delivery; reporting, statistical analysis, ad-hoc analysis and predicative analysis. The concept of Business Intelligence (BI) is brought up by Gartner Group since 1996. It is defined as the application of a set of methodologies and technologies, such as J2EE, DOTNET, Web Services, XML, data warehouse, OLAP, Data Mining, representation technologies, etc, to improve enterprise operation effectiveness, support management/decision to achieve competitive advantages. Golfarelli et al. (2004) defined BI that includes effective data warehouse and also a reactive component capable of monitoring the time critical operational processes to allow tactical and operational decision-makers to tune their actions according to the company strategy. Gangadharan and Swamy (2004) define BI as the result of in-depth analysis of detailed business data, including database and application technologies, as well as analysis practices.

They widen the definition of BI as technically much broader tools that include potentially encompassing knowledge management, enterprise resource planning, decision support systems and data mining. Berson et.al (2002); Curt Hall (1999) BI includes several software for Extraction, Transformation and Loading (ETL), data warehousing, database query and reporting, OLAP, data analysis, data mining and visualization. The BI literature lacks a universally accepted definition of BI (Pirttimaki 2007; Wixom and Watson 2010). The definitions range from one-dimensional definitions, in which BI is viewed as a set of technologies or as a

process, to multidimensional definitions, in which BI is viewed as a process, a set of technologies and a product (a detailed discussion about the BI definitions is provided in chapter two). In line with the multidimensional view, Davenport (2006) defines BI as a term which: “encompasses a wide array of processes and software to collect, analyzes, and disseminate data, all in the interest of better decision-making.” In the same way, Wixom and Watson (2010) define BI in their paper as: “a broad category of technologies, applications, and processes for gathering, storing, accessing, and analyzing data to help its users to make better decisions.” One of the main issues that are obvious in the literature is the confusion between business intelligence and competitive intelligence (CI).

In the literature, authors such as Calof and Wright (2008), Kinsinger (2007), Martinsons (1994) and Vedder et al. (1999) use the term BI to convey the concept of competitive intelligence. Competitive intelligence (CI), also known as business intelligence, is both a process and a product (Calof and Wright 2008). As a process, CI is the set of legal and ethical methods an organization uses to harness information that helps it achieve success in a global environment. As a product, CI is information about competitors’ activities from public and private sources, and its scope is the present and future behavior of competitors, suppliers, customers, technologies, acquisitions, markets, products and services, and the general business environment. CI covers the entire competitive environment (including both current and potential competitors) by collecting internal and external information to identify business opportunities and threats (Calof and Wright 2008). However, the concept of CI attained popularity only in the marketing intelligence literature together with the concept of marketing/market intelligence (Calof and Wright 2008). The most recent papers define BI as a three-dimensional concept. Shariat and Hightower (2007) characterize it as a composition of processes, technologies and products: processes for collecting and analyzing business information; technologies used in those processes; and the product as “the information (knowledge) obtained from these processes” Inspired by the BI definitions discussed, two main BI perspectives were identified and are presented in the next section.

The term “Internal” Business Intelligence covers the ability of a company to keep information from its competitors so that they may not gain a competitive advantage from their espionage activities. Theft can take the form of Industrial Espionage (IE), as defined by the Economic Espionage Act of 1996 (EEA), where trade secrets are stolen by a foreign governments or agents against domestic businesses (Fleischer, Craig, Blenkhorn, and David, 2003). Business Espionage, on the other hand, is defined by the Central Intelligence Agency (CIA) as involving the theft of trade secrets by competitors, either

foreign or domestic (Smith, 2005). This may include cases where former workers for a company take the protected trade secrets with them when they take on a new and competitive job elsewhere and use them against a previous employer. External Business Intelligence involves your company’s attempts to gain information about a competitor to gain an advantage. Based again on a CIA definition, by Smith, (2005), this is called Corporate Espionage (CE). Although the term may not seem legal, there are many perfectly ethical methods to conduct CE (Fleisher, Wright, & Tindale, 2007). Internal BI refers to the protection and utilization of internal data and external BI refers to the gathering of data and information about the competition.

According to Central Intelligence Agency CIA (Fleischer, et al. 2003) there are three types of Espionage when dealing with trade secrets, businesses intelligence and competitive advantage:

- Industrial Espionage – Foreign government vs. Domestic Business.
- Business Espionage – Foreign or Domestic Business vs. Domestic Business.
- Corporate Espionage – Legal and ethical intelligence gathering by Domestic

The Federal Bureau of Investigations (FBI), on the other hand defines the theft of trade secrets using the definitions in the Economic Espionage Act of 1996 - Economic Espionage includes industrial, business, and corporate espionage (Pooley, Lemley, & Toren, 1996). **Industrial Espionage:** Section 1831 of the Economic Espionage Act of 1996 described industrial espionage as the theft of trade secrets by a foreign instrumentality any agency, bureau, ministry, component, institution, association, or any legal, commercial, or business organization, corporation, firm, or entity that is substantially owned, controlled, sponsored, commanded, managed, or dominated by a foreign government; and/or a foreign agent any officer, employee, proxy, servant, delegate, or representative of a foreign government. An example of Industrial Espionage was the French Government, in conjunction with Air France, planting electronic listening devices in the seats in first class. The purpose of these devices was to monitor conversation between first class customers discussing business topics (Simon, 1998).

Business Espionage: Section 1832 – the theft of domestic trade secrets by a foreign or domestic business. Besides foreign governments, foreign and domestic companies are responsible for the theft of trade secrets from domestic companies. Some of the case studies that are examples of this type of espionage include (Carr, Morton, & Furniss, 2000):

- Retired Kodak employees forming a consulting business passing along Kodak internal information.
- Taiwanese Business receiving insider information on creation of labels from an employee of Avery Dennison.

- A Lockheed Martin employee hired by Boeing bringing along trade secrets

Corporate Espionage: While at first blush CE may give the appearance of something unethical, in reality there are a number of ways for companies to carry out CE that are well within the established bounds of proprietary. Many of these are actually simple methods that may prove very lucrative when properly utilized. CE is generally conducted by the employee. These are employees who gather the competitor's information as part of their normal employment process. This information can be collected in the following ways (Carr, Morton, & Furniss, 2000):

- Publications
- Conferences
- Internet
- Business Information

BI systems combine data gathering, data storage, and knowledge management with analytical tools to present complex internal and competitive information to planners and decision makers. Implicit in this definition is the idea (perhaps the ideal) that business intelligence systems provide actionable information delivered at the right time, at the right location, and in the right form to assist decision makers. The objective is to improve the timeliness and quality of inputs to the decision process, hence facilitating managerial work. Sometimes business intelligence refers to on-line decision making, that is, instant response. Most of the time, it refers to shrinking the time frame so that the intelligence is still useful to the decision maker when the decision time comes. In all cases, use of business intelligence is viewed as a proactive management system with essential components of proactive BI as shown below (Gupta, & Sharma, 2013):

3.3. Components of Business Intelligence

OLAP (On-line analytical processing): Codd, & Salley, (1993) defines OLAP as a way in which business users can slice and dice their way through data using sophisticated tools that allow for the navigation of dimensions such as time or hierarchies. Online Analytical Processing or OLAP provides multidimensional, summarized views of business data and is used for reporting, analysis, modeling and planning for optimizing the business. OLAP techniques and tools can be used to work with data warehouses or data marts designed for sophisticated enterprise intelligence systems. These systems process queries required to discover trends and analyze critical factors. Reporting software generates aggregated views of data to keep the management informed about the state of their business. Other BI tools are used to store and analyze data, such as data mining and data warehouses; decision support systems and forecasting; document warehouses and document management; knowledge management;

mapping, information visualization, and dash boarding; management information systems, geographic information systems; Trend Analysis; Software as a Service (SaaS).

Advanced Analytics: it is referred to as data mining, forecasting or predictive analytics, this takes advantage of statistical analysis techniques to predict or provide certainty measures on facts (Bose, 2009).

Corporate Performance Management (Portals, Scorecards, and Dashboards): this general category usually provides a container for several pieces to plug into so that the aggregate tells a story. For example, a balanced scorecard that displays portlets for financial metrics combined with say organizational learning and growth metrics (Andreeva, Boehm, Gaidioz, Karavakis, Kokoszkiewicz, Lanciotti, & Sidorova, 2010). Real time BI: It allows for the real time distribution of metrics through email, messaging systems and/or interactive displays (Azvine, Cui, Nauck, & Majeed, 2006). Data Warehouse and data marts: The data warehouse is the significant component of business intelligence. It is subject oriented, integrated. The data warehouse supports the physical propagation of data by handling the numerous enterprise records for integration, cleansing, aggregation and query tasks. It can also contain the operational data which can be defined as an updateable set of integrated data used for enterprise wide tactical decision-making of a particular subject area. It contains live data, not snapshots, and retains minimal history. Data sources can be operational databases, historical data, external data for example, from market research companies or from the Internet), or information from the already existing data warehouse environment. The data sources can be relational databases or any other data structure that supports the line of business applications (Andreeva et al. 2010).

They also can reside on many different platforms and can contain structured information, such as tables or spreadsheets, or unstructured information, such as plaintext files or pictures and other multimedia information. A data mart as described by (Inmon, 1999) is a collection of subject areas organized for decision support based on the needs of a given department. Finance has their data mart, marketing has theirs, and sales have theirs and so on. And the data mart for marketing only faintly resembles anyone else's data mart. Perhaps most importantly, (Inmon, 1999) the individual departments own the hardware, software, data and programs that constitute the data mart. Each department has its own interpretation of what a data mart should look like and each department's data mart is peculiar to and specific to its own needs. Similar to data warehouses, data marts contain operational data that helps business experts to strategize based on analyses of past trends and experiences. The key difference is that the creation of a data mart is predicated on a specific, predefined need for a certain

grouping and configuration of select data. There can be multiple data marts inside an enterprise. A data mart can support a particular business function, business process or business unit. A data mart as described by (Inmon, 1999) is a collection of subject areas organized for decision support based on the needs of a given department. Finance has their data mart, marketing has theirs, and sales have theirs and so on. And the data mart for marketing only faintly resembles anyone else's data mart. Beside components Business intelligence has its own systems.

3.4 Business Intelligence Systems

The role of BI systems and their influence over organizations have been subject to change. From simple, static analytical applications they have evolved into solutions that can be used in strategic planning, customer relationship management, monitoring operations, studying the profitability of products, (Negash & Gray, 2008). They are no longer regarded as a technological category only and have become the determinant of a new approach to the management of an organization (Sauter, 2010) and a new way of collecting, storing, processing, analysing, and using information (Williams & Williams, 2007). BI systems refer to decision making, information analysis and knowledge management, and human-computer interaction. Therefore, they are also often associated with systems such as MIS (management information systems), DSS (decision support systems), EIS (executive information systems), management support systems, and business / corporate performance management (O'Brien & Marakas, 2007). However, it is good to remember certain, important differences between these systems. MIS focus mainly on the automation of business processes. DSS provide techniques for analyzing information to assess potential decisions. EIS present the information in an aggregate form, and their beneficiaries are top-level management executives. Whereas, the BI goal is to provide organizations with intelligence that should be used to create competitive advantage. They combine the capabilities of different systems, which previously operated independently. BI focuses on supporting a variety of business functions, using the process approach and advanced analytical techniques (Glancy & Yadav, 2011). BI systems may be analyzed from two perspectives: technical and business (Olszak & Ziemba, 2003, 2006, 2010a). From the technical perspective they are referred to as an integrated set of tools, technologies, and software products that are used to collect heterogenic data from dispersed sources and then to integrate and analyze data to make them commonly available (Olszak, et al.2010)

They include: tools to extract, transform and load data (ETL, Extraction-Transformation-Load

tools) – are mainly responsible for data transfer from transaction systems and Internet to data warehouses;

- data warehouses – provide place for thematic storing of aggregated and already analyzed data;
- analytic tools (OLAP, On-Line Analytical Processing) – let users to access, analyze and model business problems and to share information that is stored in data warehouses;
- data mining tools – they enable to discover various patterns, generalizations, regularities and rules in data resources; tools for reporting and ad hoc inquiring – enable the creation and utilisation of different synthetic reports; and presentation layer – applications including graphic and multimedia interfaces which task is to provide users with information in a comfortable and accessible form.

From the business (organizational) perspective, BI systems mean specific philosophy and methodology that refer to working with information and knowledge, open communication, and knowledge sharing along with the holistic and analytic approach to business processes in organizations (Olszak, et al.2010). BI systems are assumed to be solutions that are responsible for transformation of data into information and knowledge, and they also create some environment for effective decision-making, strategic thinking, and acting in organizations (Negash & Grey, 2008). The value of BI for business is predominantly expressed in the fact that such systems cast some light on information that may serve as the basis for carrying out fundamental changes in a particular enterprise, that is establishing a new co-operation, acquiring new customers, creating new markets, offering products to customers (Olszak & Ziemba, 2004) and many more.

3.5 What else does Business Intelligence do?

BI assists in strategic and operational decision making. A Gartner survey ranked the strategic use of BI in the following order (Shah, 2012)

1. Corporate performance management
2. Optimizing customer relations, monitoring business activity, and traditional decision support
3. Packaged standalone BI applications for specific operations or strategies
4. Management reporting of business intelligence

One implication of this ranking is that merely reporting the performance of a firm and its competitors, which is the strength of many existing software packages, is not enough. A second implication is that too many firms still view business intelligence (like DSS and EIS before it) as an inward looking function. Business intelligence is a natural outgrowth of a series of previous systems designed to support decision making. The emergence of the data warehouse as a repository, the advances in data

cleansing that lead to a single truth, the greater capabilities of hardware and software, and the boom of Internet technologies that provided the prevalent user interface all combine to create a richer business intelligence environment than was available previously. BI pulls information from many other systems for its competitiveness.

3.6 Competitive Analysis of Business Intelligence

Competitive intelligence (CI) is a specialized branch of Business Intelligence. It is “no more sinister than keeping your eye on the other guy albeit secretly” (Imhoff, Zhang, Wolfe, & Bounoua, 2010). The Society of Competitive Intelligence Professionals (SCIP) defines CI as follows (Negash, 2004). Competitive Intelligence is a systematic and ethical program for gathering, analyzing and managing external information that can affect your company’s plans, decisions and operations (Negash, 2004). In other words, CI is the process of ensuring your competitiveness in the marketplace through a greater understanding of your competitors and the overall competitive environment. Competitive intelligence (CI) is not as difficult as it sounds. Much of what is obtained comes from sources available to everyone, including (Imhoff, 2003):

- Government websites and reports
- Online databases, interviews or surveys,
- Special interest groups (such as academics, trade associations, and consumer groups),
- Private sector sources (such as competitors, suppliers, distributors, customer) or
- Media (journals, wire services, newspapers, and financial reports).

The challenge with CI is not the lack of information, but the ability to differentiate useful CI from chatter or even disinformation

Of course, once a firm starts practicing competitive intelligence, the next stage is to introduce countermeasures to protect itself from the CI of competitor firms. The game of measure, countermeasure, and counter-countermeasure, and so on to counter to the last measure is played in industry just as it is in politics and in international competition. The question will be, “Is it really worth applying in SMEs?”

3.7 Is it really worth it? Measuring Financial Impact

3.7.1 Benefits of BI adoption in SMEs.

Given the huge amount of data that is collected by companies and the information in the public domain, conventional wisdom suggests that the company that can extract, analyze and capitalize on the information will have a strategic advantage (Love, & Irani, 2004). Love et al. (2004) suggests that as with any business

initiative, management needs to know whether the cost of the effort was worth the benefit that is, was there a tangible business advantage? Interestingly, the business community has had a difficult time determining the value of BI efforts. There are several reasons for this. The first is that, often, the executives initiate a BI effort without first calculating a projected return on investment (ROI). According to Kimball, & Ross, (2002) in a 2002 The Data Warehousing Institute (TDWI) conference survey, “only 13% of all respondents had calculated the ROI of their BI projects, and only 37% were planning to do so”. Why is this? When the 510 respondents who rated the value of BI projects as “high” or “very high” were asked what the benefits were, only two of the top 6 benefits were hard, tangible benefits (time savings, cost savings) compared to intangible benefits (single version of the “truth”, better strategy and plans, better tactics and decisions, and more efficient processes)

In another survey, the 50 top Finnish companies were polled regarding their BI practices. Here, the greatest benefits were; better quality of information, better observation of threats and opportunities, growth of the knowledge base, increased sharing of information and improved efficiency. In contrast to the previous study, cost savings and time savings were lowest on the list of benefits (Elbashir, Collier, & Davern, 2008). Therefore, it is not surprising that a ROI is difficult to determine when the perceived benefits are rather “soft”. Consistent with the above results, a Forrester research study found that “only 16 of 50 companies calculated an ROI before building a data warehouse” (Elbashir, Collier, & Davern, 2008). Note that the advantages (Elbashir, Collier, & Davern, 2008) of an integrated BI project are many. These include:

- Enterprise wide information
- Enterprise wide access
- Easy access through a single, personalized portal
- More real-time information
- Decreased costs and time associated with typical report writing
- Ability to set up more complex alerts

Studies conducted in 2003 show Return on Investment (ROI) for BI installations can be substantial. An IDC study on the financial impact of business analytics, using 43 North American and European organizations indicated a median five-year ROI of 112% from an investment of \$2 million (Negash, 2004). Return ranged from 17% to 2000% with an average ROI of 457%. However, BI budget and ROI were not found to be correlated (Negash, 2004). A wide range of the benefits for an organization emerges from the basic principles of BI. Hannula and Pirttimäki (2003) carried out a study among the large Finnish companies to find out the benefits gained from BI. The most significant benefits provided by BI activities were:

- Better quality information acquired for decision-making (95%),
- Improved ability to anticipate earlier the possible threats and opportunities (83%),
- Growth of knowledge base (76%),
- Increase of sharing information (73%),
- Improved efficiency (65%),
- easier information acquisition and analysis (57%), and
- Faster decision-making (52%).

Time-savings (30%) and cost-savings (14%) were not considered particularly important. The researchers also asked the interviewees to name one factor to describe the most significant benefit of their BI activities. The following benefits were considered to be important:

- harmonizing the way of thinking of company personnel,
- broadening understanding of business in general, strengthening strategic planning,
- increasing professionalism in acquisition and analysis of information, and
- understanding the meaning of information

The major benefits of BI, as presented by Thompson, Rust, & Rhoda (2005) are:

- Faster, more accurate reporting (81%),
- Improved decision making (78%),
- Improved customer service (56%),
- Increased revenue (49%).

Many Organizations around the world and in many different industries have been reaping the benefits of BI for years (Eckerson, 2002). A department of finance and revenue has closed its tax compliance gap by \$10 million a year while optimising customer satisfaction, thanks to a new BI solution. A major electronics retailer attributes \$1.3 million a year in fewer out-of-stock situations to a BI solution. The same solution also saves \$2.3 million a year in inventory costs due to more accurate supplier shipments. A major automobile manufacturer generated a 2,000 percent ROI on a financial BI solution that saved the firm millions of dollars by identifying repossessed vehicle loans more quickly (Wixom, & Watson, 2010). These are just a few of the many successful BI solutions at work today. Seven out of ten companies are moving to analyze their data either daily or instantly in 2006 according to Gartner, and CIO's are listing BI as their second-highest priority in 2005, (up from tenth in 2004). Gartner also forecasts that companies worldwide will spend nearly \$6 billion this year alone to gain better insight into their internal operations. SMEs can't afford to ignore the benefits of BI if they want to remain competitive. Many of the benefits of BI are intangible. Wixom, & Watson, (2010) present tangible benefits as well as those that is difficult to measure. For example, companies may eliminate software and hardware licenses and fees when they consolidate and retire data marts, or companies may reduce headcount when they replace manual reporting

processes. Other benefits, such as the enabling of new ways of doing business, are much more difficult to quantify, but may generate a competitive advantage or open up new markets for the company. The three general BI benefit factors can be described as follows (Wixom, & Watson, 2010):

3.8 BI benefit factor 1: Improvements in data support

The first factor encompasses all attributes that are connected to reporting and its improvement. For example, it includes the reduction in the overall effort concerning data analysis and reporting as well as improvements in the reports' quality and a more flexible reaction to new information needs.

3.8.1 BI benefit factor 2: Improvements in decision support

Factor 2 covers the attributes that can be associated with decision support and its improvement. It contains facts about improved business decisions through more precise as well as more current data analyses. In addition, the identification of chances and risks can be improved by using BI systems. Also the improvement in the business results loads onto factor 2.

3.8.2 BI benefit factor 3: Savings

The third factor includes statements which pertain to successes in rationalization. These include attributes regarding savings in personnel and in costs. By saving personnel and costs, competitive advantages can be achieved indirectly, either by diminishing the cost part in the income and loss statement or by having the possibility of using the saved resources in other areas.

3.9 Costs of business intelligence

Most firms today do use some form of business intelligence, although only a few operate complete BI systems. To simplify the cost discussion, consider a firm starting from scratch. According to (Wixom, & Watson, 2010) putting a BI system in place includes the following costs:

- Hardware costs. These costs depend on what is already installed. If a data warehouse is in use, then the principal hardware needed is a data mart specifically for BI and, perhaps, an upgrade for the data warehouse. However, other hardware may be required such as an intranet (and extranet) to transmit data to the user community.
- Software costs. Typical BI packages can cost \$60,000. Subscriptions to various data services also need to be taken into account. For example, firms in the retail industry buy scanner data to

ascertain how demand for their products and competing products responds to special offers, new introductions, and other day-to-day changes in the marketplace.

- Implementation costs. Once the hardware and software are acquired, a large one-time expense is implementation, including initial training. Training is also an ongoing cost as new people are brought in to use the system and as the system is upgraded. In addition, annual software maintenance contracts typically run 15% of the purchase costs.
- Personnel costs. Personnel costs for people assigned to perform BI and for IT support personnel, need to be fully considered to take into account salary and overhead, space, computing equipment, and other infrastructure for individuals. A sophisticated cost analysis also takes into account the time spent reading BI output and the time spent searching the Internet and other sources for BI.

Outside the above costs, there are already a number of studies on BI success factors (Olszak, & Ziemia, 2012). In the context of Business Intelligence systems, CSFs can be perceived as a set of tasks and procedures that should be addressed in order to ensure BI systems accomplishment. These tasks and procedures would either to be fostered, if they had already occurred, or be worked out, if they were nonexistent. Olszak, & Ziemia, (2012) cited the below Critical Success Factors as major.

3.9.1 Political

Inconsistency in policies, laws and regulations, and political instability affect BI systems accomplishment. Several associated factors that may prompt political challenge to the project are:

- Political takeover or military coup;
- War or revolution;
- Allegations of corruption causing government resignation; and
- Nationalization of assets with or without adequate compensation.

3.9.2 Legal

Legal factors include:

Unexpected changes in government policies pertinent to laws and regulations and currency conversion;

- Absence of appropriate regulatory systems;
- Rates and methods of taxation including customs, royalties, convertibility of currency;
- Role of local courts in arbitration; and
- The methods by which electricity tariffs are set and approved.

3.9.3 Cultural

Various socio-cultural background of the parties involved, various thinking processes

3.9.4 Technical

Several associated factors that may prompt technical challenge to the project are:

- Design;
- Engineering;
- Procurement; and
- Construction, equipment installation and operation of the equipment and its compatibility with accomplishment of project objectives.

3.9.5 Managerial/ organizational

Managerial or organizational factors refer to inadequate or ineffective management of the project by project sponsor or project management agency. The events in managerial factors include the following:

- Inadequate communication;
- Unclear objectives;
- Too optimistic goals in relation to project cost and schedule;
- Lack of project sponsorship;
- Unclear lines of responsibility, authority, and accountability;
- Slow and cumbersome decision-making process;
- Lack of training of the local staff for sustainability; and
- Lack of end-user participation

3.9.6 Economical

Economic factors refer to the issues influencing the economic feasibility of the project including the changes in domestic economic conditions of the recipient country or inaccurate project development plan due to unpredictable economic conditions

3.9.7 Environmental

Environmental factors refer to issues in conflict with established environmental regulations of the recipient country. This comprises pollution related issues such as noise, air pollution, water pollution, and visual disturbances and those related to natural resources such as unsustainable use of natural resources including minerals, water, land, and flora and fauna.

3.9.8 Social

Hostility due to religion, customs, and ethnicity of the project participants:

- Social uprising or riots due to ethnicity or polarization of social strata;
- Security of the stakeholders;

- Overestimation of capacity of the beneficiaries; and
- Resistance of the beneficiaries to new social values and standards or to absorb the effects of economic change or new technology.

3.9.9 Corruption

Factors which enable corruption include:

- State agencies and politicians that implement projects;
- Lenders that may favour some contractors;
- The delegation of architects, engineers, supervisors, and consultants responsible for each project;
- Panels inspecting and accepting finished projects;
- Contractors who are ready to buy projects with bribes; and
- Laws and regulations that can be misinterpreted to favour any parties.

3.9.10 Physical

Natural disaster for example fires, floods, drought, lightning, typhoon, earthquake, wars, hostilities, military coups, civil strife, and acts of terrorism dangerous to BI systems accomplishment.

4. Discussion of findings

Findings revealed that organizations which have the greatest success with BI travel an evolutionary path, starting with basic data and analytical tools and transitioning to increasingly more sophisticated capabilities until BI becomes an intrinsic part of their business culture. The article report, "Three Approaches to BI and Decision Impact", describes a three-stage process in which organizations gradually grow in analytical sophistication as their business needs and demands evolve (Baars, & Kemper, 2008):

1. Business Intelligence (IT). Organizations at this level generally approach BI as an IT-driven initiative focused on data collection and analytical tool selection. They ask "What happened?" and focus on making better business decisions through analysis of historical data.

2. Information management. At this stage organizations ask, "How are we doing against the plan, and what can we squeeze now to hit the target?" Do we have the right bullets to hit the target? Decisions become more real time as businesses bid BI tools and technology to push information to people so they can make better business decisions in the moment. This usually involves integrating data from CRM and ERP applications.

3. Extrapolative insight. In this approach, businesses add advanced analytics and predictive modeling to anticipate likely future events and capitalize on new trends or market opportunities.

These enterprises ask "What will happen next, and how can we optimize the outcome?" They not only see the future, but play a role in creating it.

Note that the advantages of an integrated BI project are many.

Watson, & Wixom, (2007) discusses some of the findings below as benefits

- Enterprise wide information
- Enterprise wide access
- Easy access through a single, personalized portal
- More real-time information
- Decreased costs and time associated with typical report writing

Business intelligence is not necessarily about tools and technologies; rather it is strategies of combining data from various sources with methodologies that make those facts solidify in a cohesive manner (Watson, & Wixom, 2007). Once the data is sourced, scrubbed, enriched, conformed, and finally housed in "access-ready" formats BI tools can make the data sing and dance.

4.1 Future of business intelligence

Liautaud, & Hammond, (2000) posited that in this rapidly changing world, consumers are now demanding quicker more efficient service from businesses. To stay competitive companies must meet or exceed the expectations of consumers (Kysar, 2003). Companies will have to rely more heavily on their business intelligence systems (Watson, & Wixom, 2007) to stay ahead of trends and future events and SMEs are not spared. Business intelligence end-users are beginning to demand Real time Business Intelligence or near real time analysis relating to their business, particularly in frontline operations. They will come to expect up to date and fresh information in the same fashion as they monitor stock quotes online (Kysar, 2003). In the not too distant future companies will become dependent on real time business information in much the same fashion as people come to expect to get information on the internet in just one or two clicks. Also in the near future business information will become more democratized where end users from throughout the organization will be able to view information on their particular segment to see how it's performing (Watson, & Wixom, 2007). So, in the future, the capability requirements of business intelligence will increase in the same way that consumer expectations increase. It is therefore imperative that companies increase at the same pace or even faster to stay competitive.

4.2 Recommendation

SMEs are perfect candidates for an incremental approach to BI. To be agile and compete with larger rivals, managers and business users at midsize

companies need targeted, timely and accurate information – information that can successfully drive strategic business decisions. But because they have limited IT staff and budgets, smaller firms need a practical solution that enables them to deploy components tactically and incrementally. These businesses should “think big” – that is, draw on the conceptual frameworks of larger companies – yet scale their approaches to fit a company with fewer resources. For a Business Intelligence project’s implementation to be successful and to bring tangible business benefits to SMEs in the future, it is worthwhile to meet some of the below basic conditions:

- BI system must be a part of the company's business strategy. It must correspond to the real needs of users and support key processes and business decisions at all levels of management (strategic, tactical and operational). To do this the knowledge about the BI system opportunities in the context of business challenges becomes indispensable for an enterprise. A good understanding of decision-making processes is also required, because only then the BI system can be used effectively;
- Managing the BI system implementation ought to be centralized, but all of its prospective users should be involved in the implementation. Only such a situation will enable users to adapt the BI system functionality to the individual needs while ensuring the proper conduct and success of implementation;
- The implementation of the BI system requires appropriate knowledge and skills for the BI implementation. A competent project team, consisting of managers, employees and IT specialists, is essential;
- BI system implementation project must have a sponsor who is positioned in the organizational hierarchy as high as possible. Commitment of managers, especially of the board, in the process of choosing and implementing BI systems is required. This will ensure adequate resources and be a clear signal to employees that management attaches due importance to the project;
- BI system requires permanent development and adaptation to new challenges and expectations of an enterprise. The consequence of BI system non-development is its depreciation and withdrawal;
It is necessary for users to be able to use the BI system. This can be provided by staff training and a very high-friendliness of the system; and
- The cost of BI implementation must cover the costs of technology, but also account for measures to establish a project team, technical support, and substantive support, and change management, employees training as well as maintaining and developing the BI system in the

future. Otherwise, the enterprise receives a powerful tool that no one will use.

5. Conclusions

Nowadays, BI becomes an essential part of any enterprise, even SMEs. This necessity is caused by the increasing data volume indispensable for decision making. Existing solutions and tools are mostly, aimed at large-scaled enterprises; thereby they are inaccessible or insufficient for SMEs because of high price, redundant functionality, complexity, and high hardware and software requirements. SMEs require solutions with light architectures that, moreover, are cheap and do not require additional hardware (Abadi, et al. 2003) and software. Business intelligence is very much worth it in SMEs. The research results indicate that the use of a BI system will result in a business success only if the BI users, on a regular basis, develop business and decision-making processes, recognize their needs, assist their modeling and oversee the completion of a project as well as actively participate in the implementation of new BI components. The knowledge and skills of a project team and BI systems users are of primary importance. It can be summarily concluded that business intelligence is a cutting edge strategic asset in SMEs and again it is really worth adoption by SMEs in Zimbabwe as return on investment (ROI) is guaranteed when all the necessary procedures are taken.

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