Building and Sustaining an Ethical Culture

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President and CEO
Center for Ethical Business Cultures
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About the Center for Ethical Business Cultures

Mission

To assist business leaders in creating ethical and profitable business cultures at the enterprise, community and global levels

Background

✓ 33 year old nonprofit organization
✓ Began partnering in 1988 with University of St. Thomas
✓ Member of the Advisory Group to the US Sentencing Commission
✓ Advises Boards and Executive Leaders on “Tone at the Top”
✓ Building a Bridge Between Thought and Practice Leadership

Why is it Important?

Organizations that build an ethical culture:

✓ Do it because it’s the right thing to do
✓ Outperform organizations that don’t
✓ Reduce their exposure to ethical lapses that cause breakdowns
Goals for the Day

- To develop an understanding of individual and organizational ethics and values in the workplace.
- To focus on the leader’s role in achieving performance goals within the highest standards of integrity and ethical behavior.
- To explore the importance of aligning systems in the organization to drive the desired behavioral expectations.

Organizing the Day

- Examining Ethical Approaches
  - “Happy Hills”
- Linking Personal & Organizational Ethics
  - The Parable of the Sadhu
- Scanning the Environment
- When Values Collide
  - The Letter of the Law Case
- Building and Sustaining Ethical Cultures
As the new mayor of Happy Hills, would you direct that this sign be:

☑ Taken down or altered?

or…

☑ Not taken down?
Ethical Approaches

- **Consequences**
  - What will be the effects of the proposed action on any stakeholders?

- **Absolute Principles**
  - Will the proposed action be in alignment with universal ethical principles?

- **Synthesis**
  - Both stakeholder consequences and absolute principles must be considered.

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Ethical Approaches

- Beyond the Absolute Principles and Consequential approaches:
  - Duties – Obligations to a community of common interests, i.e. fiduciary responsibility
  - Rights – Fair distribution of opportunities and wealth or basic freedoms and liberties
  - Interests – (Consequential - Utilitarian) Harms and benefits to the interest of parties affected
  - Virtue – (Absolute Principles - Kantian) A positive trait of character including prudence, impartiality, courage, justice, and belief/trust
Linking Personal & Organizational Ethics
The Parable of the Sadhu

The Parable of the Sadhu

As McCoy, would you have carried the sadhu to safety?
or...
Left him to his own resources?
“Teleopathy”

- The unbalanced pursuit of purpose in either individuals or organizations.
- This mindset is a key stimulus to which ethics is a practical response.
- The principal symptoms of teleopathy are fixation, rationalization, and detachment.

Teleopathy

- **Fixation** on tangible goals or purposes without moderation
- A tendency to *rationalize* or even deny responsibilities and realities that might impede the accomplishment of those goals or purposes
- A general separation of the ethics of business goals from the ethics of everyday life leads to emotional *detachment* from the full human implication of pursuing those goals.
Antidotes to Teleopathy

- **Fixation** to perspective...understanding that the goals we set for ourselves are part of a larger mission
- **Rationalization** to frankness...practice, practice, practice telling the truth when exaggeration or denial appear attractive
- **Detachment** to engagement ... learning to keep the “head” (what we have to do) and the “heart” (how we do it and who is affected) in healthy communication

Scanning the Environment
Who Do You TRUST?

How much do you TRUST each institution to do what is right? (2008 - 2011)

<table>
<thead>
<tr>
<th>Percent</th>
<th>America's US/Canada/Brazil</th>
<th>Europe France/Germany/ Russia</th>
<th>Asia China/Japan/ India</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business 2008</td>
<td>58/49/61</td>
<td>30/35/42</td>
<td>54/61/74</td>
</tr>
<tr>
<td>Business 2009</td>
<td>36/41/67</td>
<td>30/34/52</td>
<td>62/63/71</td>
</tr>
<tr>
<td>Business 2010</td>
<td>54/na/62</td>
<td>36/40/42</td>
<td>62/57/67</td>
</tr>
<tr>
<td>Business 2011</td>
<td>46/na/81</td>
<td>48/52/41</td>
<td>61/53/70</td>
</tr>
<tr>
<td>Govt. 2008</td>
<td>39/49/22</td>
<td>35/27/38</td>
<td>79/45/49</td>
</tr>
<tr>
<td>Govt. 2009</td>
<td>30/51/51</td>
<td>34/36/48</td>
<td>72/45/42</td>
</tr>
<tr>
<td>Govt. 2010</td>
<td>46/na/39</td>
<td>43/43/38</td>
<td>74/42/43</td>
</tr>
<tr>
<td>Govt. 2011</td>
<td>40/na/85</td>
<td>49/33/39</td>
<td>88/51/44</td>
</tr>
</tbody>
</table>

Source: 2011 Annual Edelman Trust Barometer

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Confidence in Leaders

Source: Harris Poll March 3, 2010

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Ethical Breakdowns in

- Worldcom
- Enron
- Tyco
- HealthSouth
- Global Crossing
- Arthur Anderson
- Adelphia
- Morgan Stanley
- Putnam
- Qwest
- UnitedHealth Group
- BUCA
- Siemens
- Hewlett Packard
- Parmalat
- Cendant
- Computer Associates
- KPMG
- Hyundai Motors
- Boeing
- American Red Cross
- Johnson & Johnson
- Purdue Pharma
- Bristol Myers-Squibb
- Google & Yahoo (China)
- Toyota Safety Recalls
- Financial Services Sector Meltdown
- Royal Dutch Shell
- BP Amoco Oil Spill
- Denny Hecker
- Tom Petters
- Bernie Madoff
- Societe Generale
- PetroChina
- AGA Medical Co.
- Ahold
- Bear Stearns
- Sanlu
- Morgan Stanley
- Putnam
- Qwest
- UnitedHealth Group
- BUCA
- Siemens
- Hewlett Packard
- Parmalat
- Cendant
- Computer Associates
- KPMG
- Hyundai Motors
- Boeing
- American Red Cross
- Johnson & Johnson
- Worldcom
- Enron
- Tyco
- HealthSouth
- Global Crossing
- Arthur Anderson
- Adelphia
- Morgan Stanley
- Putnam
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- UnitedHealth Group
- BUCA
- Siemens
- Hewlett Packard
- Parmalat
- Cendant
- Computer Associates
- KPMG
- Hyundai Motors
- Boeing
- American Red Cross
- Johnson & Johnson

How Do You Measure-Up?

Rating the honesty and ethical standards of people and professions (very high/high):

- Nurses: 81%
- Medical Doctors: 66%
- Policeman: 57%
- Clergy: 53%
- Bankers: 23%
- Lawyers: 17%
- Business Executives: 15%
- State Officeholders: 13%
- Congressman: 9%
- Car Salesmen: 7%

Two Languages of Business

Misconduct at Work

Source: Ethics Resource Center's 2009 National Business Ethics Survey
The Cost of Ethical Breakdowns

2010: typical organization loses 5% of annual revenues (estimated value ~ $2.9 trillion worldwide)

2008: U.S. organizations lose 7% of annual revenues (estimated value ~ US$994 billion)

2006: U.S. organizations lose 5% of annual revenues (estimated value ~ US$652 billion)

Typical fraud timeframe (from the time it began to the time it was discovered): two years

27% of fraud cases were corruption
46% of cases detected by tips

Source: ACFE 2010 Report to the Nation on Occupational Fraud & Abuse

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Cheating Among MBA Students

- 56% of MBA candidates surveyed admitted they had cheated at least once
  - “culture of greed within MBA schools”
  - “get it done at all costs”
  - “shifting priorities from meeting customers’ needs to protecting shareholders profits”
- Over 16 years, on every study of cheating, except one, business students led the way

Source: McCabe, Butterfield & Trevino, September 2006

Driving Ethical Culture:
*The Legislative/Regulatory Response*

- Sarbanes-Oxley Act of 2002
- Public Company Listing Exchanges
- United States Sentencing Commission
- Dodd-Frank Act of 2010
- SEC Rule Making (2011-2012)
### A Collective View: The Legislative/Regulatory Response

| Setting the “Tone at the Top” | Board Independence |
| Ethical Culture |  
| Codes of Conduct |  
| Conflicts of Interest |  
| Disclosure/Transparency |  
| Whistleblower Rewards |  
| Audit |  
| Compensation |  
| Nominating-Governance |  
| Consultant Independence |  
| Audit and Tax |  
| Compensation |  
| Shareholder Access |  
| Executive Compensation |  

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### Legislative/Regulatory Theme

“…requirement that an organization shall promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.”

But you can’t legislate integrity!
When Values Collide
Letter of the Law Case
Adapted by Jon Pekel From A True Story Fictionalized by Doug Wallace

Key Questions

- Who are the stakeholders?
- What are the conflicts?
- What are the key issues?
- What are the choices?
- What’s the decision process?
What’s the Decision Process?

Testing the decision:
✓ Is it legal?
✓ Does it fit the organization’s values and comply with its conduct standards?
✓ Does it create harm or benefit (to a few or to many)
✓ What does my ethical compass say?
✓ Am I comfortable discussing my decision in the public eye?

Creating an ethical advantage:
✓ Have I identified and considered the interests of the affected stakeholders?
✓ Have I modeled behavior that I would want replicated?
✓ Am I appropriately using the organizational systems to reinforce the desired behavior?
What is an Ethical Culture?

- Based on Integrity
- Discerns and chooses right versus wrong
  - Laws and Regulations
  - Societal Standards
- Reaches for the higher standard in the gray areas when all options seem right

Characteristics in Building & Sustaining an Ethical Culture

- Values Driven
- Leadership Effectiveness
- Balancing Stakeholder Interests
- Market Based
- Ethical Culture
- Law Based
- Corporate Conscience
- Process Integrity
- Long-term Perspective
- Assessment

Source: Based on Chapter 2 “Mindsets & Culture” in Conscience and Corporate Culture. Copyright © Kenneth E. Goodpaster.
Laying the Foundation

- Mission
  - Purpose
- Vision
  - Image of the future
- Values
  - Principles that guide behavior
- Ethics & Compliance Codes
  - Legal and regulatory compliance and beyond

Shaping Organizational Culture

- Values
  - The shared norms and beliefs of the organization that define acceptable behavior
  - Inspirational and directional in nature
  - Gives individuals a context to reflect on how their personal values align

Ethics and Compliance Codes of Conduct

- The standards of behavior established to insure compliance with the law, regulations, and rules
- Prescriptive in nature with specific well defined expectations of behavior
Federal Sentencing Guidelines

- Established by the United States Sentencing Commission (USSC) in 1991 with focus on compliance
- Imposes fines, sentencing to probation, orders of restitution and public notices of conviction
- Offers incentives for organizations to “do the right thing”
- Updated to emphasize ethical conduct in 2004

The Seven Minimum Steps

1. Establish standards and procedures
2. Make high-level individuals responsible
3. Exercise due care in delegating authority
4. Provide communication and training
5. Utilize monitoring, auditing, and reporting
6. Consistently enforce through discipline
7. Take appropriate corrective action
Oversight & Management
Roles and Responsibilities

Separate attention now given to the roles and responsibilities of three types of organizational officials:

- Members of the governing authority (i.e., Board)
- Executives comprising an organization’s managerial leadership (i.e., “high-level personnel”)
- One or more specific individual(s) having day-to-day operational responsibility for an organization’s compliance and ethics program

The 1st Element
Laying the Foundation

- Data Illustration:

<table>
<thead>
<tr>
<th></th>
<th>Executive</th>
<th>Manager</th>
<th>Frontline</th>
</tr>
</thead>
<tbody>
<tr>
<td>The behavior of the people I work with is consistent with my company’s mission, vision and values.</td>
<td>75%</td>
<td>63%</td>
<td>57%</td>
</tr>
</tbody>
</table>

Source: Gantz Wiley Research WorkTrends 2008
Modeling Ethical Behavior is Crucial

- Leadership is the key ethical culture factor
- Leaders must set the tone by “talking the talk” and “walking the talk”
- Top management is generally perceived to exert more pressure on “getting the results” and not on “how the results are achieved”
- This translates into get the results “at all costs.” “The ends will justify the means!”

The 2nd Element

Effective Leadership

- Data Illustration:

  *My senior management supports and practices high standards of ethical conduct.*

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<thead>
<tr>
<th>Executive</th>
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</tr>
</thead>
<tbody>
<tr>
<td>78%</td>
<td>73%</td>
<td>68%</td>
</tr>
</tbody>
</table>

Source: Gantz Wiley Research WorkTrends 2008
The 2nd Element
Effective Leadership

Data Illustration:

Where I work, ethical issues and concerns can be discussed without negative consequences.

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<tbody>
<tr>
<td>77%</td>
<td>72%</td>
<td>62%</td>
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Source: Gantz Wiley Research WorkTrends 2008

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Your Organization

Balancing Stakeholder Interests

Community
Investors
Guests
Government-Regulatory
Environment
Employees
Suppliers
Competitors

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The 3rd Element
Balancing Stakeholder Interests

Data Illustration:

My company strives to serve the interests of multiple stakeholders not just the shareholders (financial performance).

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<tr>
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<td>65%</td>
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</tbody>
</table>

Source: Gantz Wiley Research WorkTrends 2008

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The 4th Element

Process Integrity

- Data Illustration:

Where I work, people do not “get ahead” unless their behavior clearly demonstrates my company’s values.

<table>
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<th>Executive</th>
<th>Manager</th>
<th>Frontline</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>67%</td>
<td>57%</td>
<td>50%</td>
</tr>
</tbody>
</table>

Source: Gantz Wiley Research WorkTrends 2008

Impact of Ethics

U.S. Employees

Source: Kenexa WorkTrends™ 2008

Note: values represent percent favorable
Building the Ethical Culture

- Linking & Aligning Mission, Vision, Values and Ethics & Compliance
- Leadership
- Education & Training:
  - Governing Authority
  - Senior Management
  - Mid Level Managers
  - Front Line Employees
- Connecting systems & incentives to values
- Surveying for feedback

Questions?