

8

Organizational Culture



Damien Dovarganes/Associated Press

Learning Outcomes

After reading this chapter, you should be able to do the following:

- Examine how organizational culture drives ethical behavior.
- Analyze best practices for developing an ethical culture.
- Evaluate the eight criteria required for an effective ethics and compliance program.

Introduction

Target's Struggle with Ethical Culture

After being one of three U.S. retailers recognized for exemplary ethical standards and practices for seven consecutive years, Target was not included on Ethisphere Institute's 2014 World's Most Ethical Companies list (Adams, 2014). Ethisphere Institute conducts a survey of large public and private international companies and publishes the annual list in its magazine. Ethical culture is a component in ranking the most ethical companies, looking for the adoption of a values-based culture in the organization, workforce acceptance of the culture, and employee behavior according to the ethical culture.

Target's fall from the list comes after a 2013 data breach of customer credit card data during the Christmas shopping season. Even with extensive data security measures in place, a Russian hacker accessed customer credit card and personal information from purchases made from November 27 to December 15. Reports indicate that Target received initial warning of malware as early as November 30, but did not take action until enforcement agencies contacted the company two weeks later. Most customers learned of the leaking of their sensitive data from media news outlets on December 18, one day before Target released a press statement asserting that "Target alerted authorities and financial institutions immediately after it was made aware of the unauthorized access, and it is putting all appropriate resources behind these efforts" (Target, 2013, para. 3). As more information emerged, the company reported the unauthorized access to credit card or personal data of over 110,000 customers.

The manner in which the large retailer handled the data breach crisis demonstrates an organizational culture that ignored warnings, failed to tell customers all available information, and lacked empathy for customer concern of financial harm (Levin, 2014). The investors, employees, managers, and media considered that the organizational culture of Target had become too controlling and unresponsive to new information. The chief information officer (CIO) accepted responsibility for the failure of data security and resigned from the company. In response to shareholder demands for greater accountability, a new chief executive officer (CEO) and some board members were appointed in 2014.

Why is the focus on Target's organizational culture after this crisis? Culture matters in business. A healthy culture allows employees to live their values and perform without fear of retaliation, whereas dysfunctional cultures lead to poor decisions, lower performance, and greater risk of ethical misconduct scandals (Gebler, 2012). Chapter 1 describes ethical culture as the degree to which an organization is committed to ethical responsibilities, with expectations for appropriate behaviors of its employees and suppliers. An ethical organization stresses the incorporation of values in its strategic planning in order to develop a values-based culture. United Launch Alliance is an example of a company that integrates values throughout the organization and represents a basis for their ethical programs.

Chapter 7 examined ethical leadership and its role in creating an ethical culture. A company with a strong ethical culture makes appropriate behavior a priority through leadership, fair policies, open discussion of ethics and incentives for ethical behavior (Treviño, Weaver, Gibson, & Toffler, 1999). Companies with an ethical culture have formal business ethics programs that include codes of conduct, ethical training, and reporting mechanisms for misconduct. While an ethical culture denotes the values, norms, and artifacts of an organization, an **ethical climate** refers to employees' shared perceptions of "ethically appropriate behavior and

knowledge of procedural steps to address an ethical issue” (Kuntz, Kuntz, Elenkov, & Nabirukhina, 2013, p. 319). Ethical climate relates to the collective personality of the organization, made up of the employees’ ethical attitudes, views, and decision-making processes (Ethics Resource Center, 2009).

Building on the concept of ethical leadership, this chapter focuses on organizational culture as a powerful driver of workplace behavior. An ethical culture can incentivize appropriate behaviors in business. The following material describes how an ethical culture can overcome informal group pressures for misconduct, how to measure the strength of a company’s ethical culture, and steps to develop a culture that promotes ethics in an organization. Finally, the components of an organizational ethics program provide a framework for supporting an ethical culture. These elements reinforce the importance of having an ethical leader who will promote the company’s ethical culture.

8.1 Organizational Culture Drives Ethical Behavior

Every organization with employees has a culture, sometimes termed corporate culture or company culture, which drives employee behavior. Culture in an organization can be described as “how we do things around here” (Gebler, 2012, p. 7). **Organizational culture** refers to “the pattern of shared values and beliefs that help individuals understand organizational functioning and thus provide them with the norms for behavior in the organization” (Deshpande & Webster, 1989, p. 4). Therefore, the culture of an organization consists of shared basic values, behavioral norms, and visible artifacts that guide behaviors and decision making (Homburg & Pflesser, 2000). An ethical culture founded on values will stress expectations for appropriate behaviors of its employees and suppliers.

Values, Norms, and Artifacts of an Ethical Culture

Shared basic values are basic assumptions outlining desirable ends and means that a group has invented, discovered, or developed, and that have worked well enough to be considered valid, and therefore, are taught to new members. Schein (1984) views shared values of an organization in two ways: 1) overt, espoused values, and 2) values that are taken for granted.

The first relates to stated values that the company strives to follow. Organizations choose values that reflect the history, heritage, and influence of the founders on the company’s value structure. The innovative furniture company, Herman Miller, identifies operational values that include curiosity and exploration as “two great strengths we take from our heritage of research-based design” (Herman Miller Inc., 2014b, Curiosity & Exploration section, para. 1). The core values of Heinz include operational and ethical orientations, such as team building and collaboration, vision, innovation, results, and integrity (see Figure 8.1).

Values that are taken for granted, on the other hand, are considered espoused values that, over time, transform into underlying assumptions about how things really happen in the organization. These assumptions reflect the organization’s relationship to the environment, how to interact with others, whether to trust others, and how to define truth. Target espoused

values of great customer service with a mission to deliver “outstanding value, continuous innovation, and exceptional guest experiences by consistently fulfilling our Expect More. Pay Less.® brand promise” (Target, 2014, Our mission section, para. 1). Despite this mission, the company appeared to have underlying assumptions about avoiding problems in order to make sales targets (Levin, 2014).

Figure 8.1: Heinz core values

Heinz stresses operational and ethical principles in its list of core values.



Source: Heinz. (2010). *Global code of conduct*. Reprinted with permission.

Norms are expectations of desirable behavior found in the policies and procedures that guide organizational decisions and actions. Companies express norms as principles for acceptable behavior. Chapter 1 defines principles as the rules or standards that inform actions and thinking. Heinz builds on its values to offer three guiding principles for employee behavior: 1) “compliance with applicable laws and regulations,” 2) “no conflicts with Heinz’s best interests,” and 3) “adherence to high ethical standards” (Heinz, 2010, p. 6). Google’s ethical code includes the expected behavior of making money without being evil, which is the foundation for several core principles to guide the company’s conduct, such as “democracy on the web works” and “great just isn’t good enough” (Google, 2014, para. 5, 11). Stated organizational principles represent a company’s preferred behaviors rather than the informal norms followed by most of its employees. Target’s data security protocol would have prevented continued data loss after the initial breach if its policies and procedures were indeed a company norm.

Artifacts are tangible expressions of shared values and norms and include a company's architecture, technology, manner of dress, rituals, documents, and stories (Schein, 1984). A company's code of conduct is an example of an artifact. Heinz incorporates its story to demonstrate company values in its global code of conduct:

It is, and has always been, the policy of H. J. Heinz Company to maintain the highest level of professional and ethical standards in conducting its business affairs. The Company places the highest importance on our reputation for honesty, integrity, and high ethical standards. It is a reputation that originated with our founder, Henry John Heinz, who used clear bottles for his products, unlike his competitors, so that customers could see that Heinz's products stood for quality and were not made with cheap fillers. (Heinz, 2010, p. 5)

Source: Heinz. (2010). Global code of conduct. Reprinted with permission.

Social media postings are becoming a form of artifact, as their content often reflects a company's espoused values. Cisco communicates company values through a public policy blog to discuss the company positions on issues that are important to their business (Cisco, 2013). These social media postings can also reflect underlying assumptions of company values. For example, the tweets and Facebook page of the cofounder of the mobile dating app, Tinder, as well as the company's own Twitter account, included statements calling women "sluts" and "whores" are now evidence in a sexual harassment lawsuit (Bercovici, 2014). A Target corporate employee's post blasting the company for an unproductive workplace culture required a response from Target's Chief Marketing Officer Jeff Jones. Jones said, "While we would have preferred to have a conversation like this with the team member directly, speaking openly and honestly, and challenging norms is exactly what we need to be doing today and every day going forward" (Malcolm, 2014, para. 6).

Importance of an Ethical Culture

An ethical culture that drives appropriate employee behavior is valuable to an organization. Chapter 4 established the importance of an ethical organizational culture as it relates to compliance with national guidelines and regulations, but regulatory compliance is not the only benefit. A strong ethical culture creates greater organizational commitment, stronger job satisfaction, and higher performance in employees. The ethical culture of an organization can incentivize employees' behaviors, align the informal culture of the organization with formal policies and procedures, and attract and retain a talented workforce.

Complying With Regulations

In response to the accounting scandals in the early 2000s, the U.S. Securities Exchange Commission equated a strong ethical culture with good governance. For example, the 2004 amendment of the U.S. Federal Sentencing Guidelines for Organizations (FSGO) includes a requirement for companies to "promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law" (United States Sentencing Commission, 2013, p. 497). Companies can avoid monetary fines and sanctions by committing to promote honesty and integrity throughout the organization.

Other countries have similar requirements in their company or have established anti-corruption legislation. The U.K.'s Companies Act 2006 requires the board of directors to

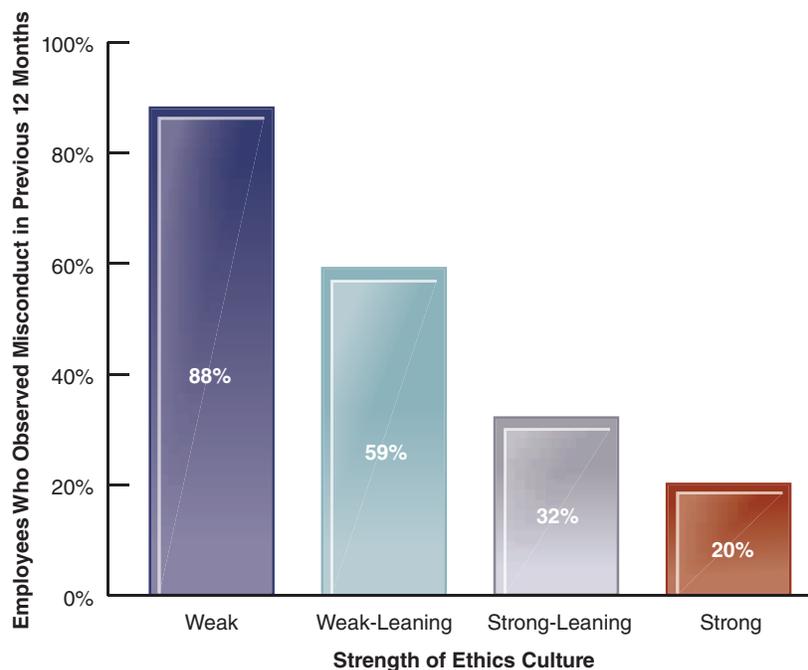
encourage a culture that considers the long-term consequences of a business on its employees, suppliers, consumers, and the environment (Casson, 2013). Yet many of the European nations continue to focus on technical aspects of director or top management responsibilities instead of the behavioral standards. The Organisation for Economic Co-operation and Development Guidelines for Multinational Enterprises (2011b) stress the need for an ethical culture built on a strong corporate governance procedure. The Belgian Directors' Association (GUBERNA) provides a guide for behaving with integrity with advice such as, "A director participates in the development and promotion of a culture of honesty" (Casson, 2013, p. 25).

Increasing Ethical Behavior

There is a proven link between an ethical culture and pressure to engage in ethical behaviors in the workplace. Studies have shown that an organizational culture that supports ethical values generates higher perceptions of honesty, lower pressures to act unethically, lower observance of misconduct, and higher reporting of misconduct (Basran, 2012; Basran & Webley, 2012; Ethics Resource Center, 2010). See Figure 8.2 for findings of the 2013 National Business Ethics Survey® of the Ethics Resource Center on the relationship of ethical culture strength and observed misconduct. The study of U.S. workers found that 88% of employees observed misconduct when their company has a weak ethical culture, significantly more than the 20% of employees who witnessed misconduct in companies that value ethical performance and build strong cultures (Ethics Resource Center, 2013b).

Figure 8.2: Relationship of ethical culture strength and observed misconduct

More employees observe unethical behavior in companies with a weak ethical culture than those with strong ethics programs.



Source: National Business Ethics Survey of the U.S. Workforce. (2013). Arlington, VA: Ethics Resource Center. Reprinted with permission.

Studies in the United Kingdom, Germany, France, Italy, and Spain have discovered results that are similar to those of the U.S. study. In the United Kingdom, 70% of workers with unsupportive ethical cultures observed misconduct (Basran & Webley, 2012). Almost half of the employees surveyed in the four countries in continental Europe observed misconduct when their employer had a weak ethical culture, whereas only 18% of employees with a strong ethical climate witnessed unethical behaviors (Basran, 2012).

Aligning Informal Culture of Groups

Ethical companies are able to align the informal culture that guides employees' behavior with the formal components of an ethical culture. Recall from Chapter 1 that informal culture is the mechanism by which employees "learn the 'true values' of the organization" (Bazerman & Tenbrunsel, 2011a, p. 117) through employee stories, observations, and experiences, which may conflict with organizational values. Formal components, on the other hand, include structures, policies, decision-making processes, and ethics training. The informal culture reflects the way things are really done—and is trusted by employees more than formal written standards. Therefore, informal cultures have a greater influence on ethical behavior in the workplace.

Financial and time pressures heavily influence informal cultural norms that conflict with the formal components of an ethical culture. For example, in a study of Swedish auditors, Svanberg and Öhman (2013) found that informal norms can affect audit quality when auditors experience time and budget pressure from their company or client. Audit firms bid for contracts that often result in tight deadlines. Auditors then deviate from formal procedures by accepting weak client explanations, endorsing a required audit step without completing the work or noting the omission of procedures, and shifting time to non-chargeable areas of the audit or to another client.

Svanberg and Öhman (2013) found that audit firms accept the unethical practice of shifting time primarily because auditors believe such misconduct will not be detected nor punished. Shifting time to non-chargeable areas of the audit or another client has become an informal industry norm. Treviño et al. (1999) found that employees' perceptions that the company consistently follows formal codes, policies, and procedures has the greatest influence in preventing the establishment of informal norms that lead to unethical behavior. Therefore, an ethical culture is required for the formal elements to be part of the larger informal culture to support ethical conduct every day (Treviño & Brown, 2004).

Attracting a Talented Workforce

Company culture influences how employees describe where they work, understand the business, and see themselves as part of the organization (Hansen, 2011). A **moral misalignment** occurs when an employee feels that there are ethical or moral differences between how the company and that individual believe the firm should operate, often becoming a signal to leave the workplace and seek employment elsewhere (Smith, 2013). Employees are less likely to leave a company when an organization's values to respect employees provide for ethical labor practices in the organization (Stewart, Volpone, Avery, & McKay, 2011). Therefore, building a strong ethical culture is key to attracting talent that, in turn, determines a business's success.

Assessing the Strength of an Ethical Culture

Potential and current employees of an organization should take into consideration its ethical culture to avoid moral misalignment. However, measuring the strength of an organization's ethical culture is challenging. As demonstrated by the Chapter 7 example of Enron's use of inspirational quotes on telephone notepads to promote the company values, ethical commitment is much more than simply hanging a plaque on the wall or having the CEO give motivational speeches. Underlying ethical assumptions are not explicit. See *Checklist: Ethical Health Assessment—How Ethical Is Your Organization?* for sample questions that could uncover implicit norms and the perception of ethical culture strength.

Checklist: Ethical Health Assessment—How Ethical Is Your Organization?

	YES	NO
• Is there a general understanding of what is correct conduct in your organization?	<input type="checkbox"/>	<input type="checkbox"/>
• Do you feel that your organization has a culture that encourages openness between management and employees?	<input type="checkbox"/>	<input type="checkbox"/>
• Are there rewards for employees who demonstrate appropriate ethical behavior?	<input type="checkbox"/>	<input type="checkbox"/>
• Do you feel that employees know how to act ethically during crises?	<input type="checkbox"/>	<input type="checkbox"/>
• Do employees treat customers fairly and honestly?	<input type="checkbox"/>	<input type="checkbox"/>
• Do employees treat each other with respect and honesty?	<input type="checkbox"/>	<input type="checkbox"/>
• Are there role models in the organization who demonstrate ethical decision making?	<input type="checkbox"/>	<input type="checkbox"/>
• Do employees receive constructive criticism on how to improve ethical conduct?	<input type="checkbox"/>	<input type="checkbox"/>
• Are employees reprimanded for violating the organization's ethical standards?	<input type="checkbox"/>	<input type="checkbox"/>

Source: Modified from Ferrell, L., & Ferrell, O.C. (2009). *Ethical business*. New York: DK Publishing, p. 49.

Questions to Consider

1. What additional questions may uncover the ethical culture of an organization?
2. Which, if any, of these questions are seeking confirmation of the ethical climate (perceptions) rather than the ethical culture (values, norms, and artifacts)?
3. How could management measure the ethical health of an organization other than survey questions?

The ethical strength of a business may depend on certain organizational characteristics. As shown in Table 8.1, the Ethics Resource Center (2010) has found that large organizations with a highly unionized workforce are more likely to have a weaker ethical culture. Labor unions can exert economic pressure on employers to restrict enforcement of ethical principles, limiting the effectiveness of a formal organizational ethics program. A historical example is the reluctance of U.S. labor unions to integrate racial diversity in the workforce in the 1940s by striking when companies hired African American workers (Bowie & Dunfee, 2002). The Ethics Resource Center finding is not supported by other studies that show that large firms have more resources for implementing formal ethical programs (Ardichvili, Jondle, & Kowske, 2012; Sweeney, Arnold, & Pierce, 2010; Zeng & Luo, 2013). However, some scholars suggest that smaller firms may be more flexible in responding to changing ethical issues (Jones, 1999; Perrini, Russo, & Tencati, 2007).

Ownership structure appears to influence the ethical culture strength of an organization in the United States, but this may not always be the case in other countries. One study revealed that family-managed companies express a greater ethical focus than nonfamily businesses do (Blodgett, Dumas, & Zanzi, 2011). In China, the socialist political structure mandates ethical responsibilities of state-owned enterprises to provide for employees, including housing, pensions, and healthcare. Foreign-owned enterprises operating in China focus their ethical programs on the Chinese government's social development goals in order to gain legitimacy in the Chinese market (Chen & Touve, 2011). Therefore, Gao (2009) found no difference in ethical focus and performance by state-owned or foreign companies.

Table 8.1: Company characteristics influencing ethical culture strength

More Likely to Have Strong or Strong-Leaning Ethical Cultures	More Likely to Have Weak or Weak-Leaning Ethical Cultures
Non-unionized workers	Highly-unionized
Fewer than 500 employees	500+ employees
Privately-held	Publicly-traded
Have employee-owners	Employees do not hold stock

Source: The importance of ethical culture: Increasing trust and driving down risks. (2010). Arlington, VA: Ethics Resource Center. Reprinted with permission.

To assess the ethical health of an organization, it is important to look beyond the printed values and stated norms. Consider the examples of Enron and Target that strived to demonstrate an ethical culture with values statements, policies and procedures for appropriate behavior, and public statements of a commitment to ethics. Yet, both organizations realized ethical misconduct disasters that created financial hardship and reputational damage. Were there apparent signs that these organizations accepted behavior that deviates from ethical standards? In the case of Enron, Sherron Watkins described two instances in which employees who had protested accounting and financial reporting practices experienced retaliation, were reassigned to less attractive positions, or were pushed out of the company. These actions sent the message that at Enron, "bad behavior was subtly rewarded, and good behavior was punished" (Beenen & Pinto, 2009, p. 280).

Signs pointing to a weak ethical culture at Target include the disgruntled employee's social media posting and dismissals of the CIO after the breach of policies that protect customer data. Whereas the ethical misconduct at Enron brought the company to bankruptcy, Target may be able to reposition its internal culture and ethical reputation over time. According to the National Retail Federation, Target is the third largest mass merchandiser in the United States (Schulz, 2014). One Forbes contributor stated, "Target has a long road ahead of it. It has some time to make things right. Its cash position seems solid and its debt is reasonable" (Rosenblum, 2014, para. 11).

To avoid ethical misconduct disasters, company management should regularly consider the informal character of the organization and the underlying assumptions shaping its ethical culture. Demonstrating a commitment to ethics and compliance in order to meet regulatory guidelines is not enough to avoid the financial and reputational damage from unethical business practices. Managers must continually assess their organization's ethical climate in order for employees to perceive that the company expects ethical behavior. Some measurements include observable negative actions (e.g., arrests or terminations for noncompliance and misconduct), reports of unethical actions (e.g., employee, customer, or supplier complaints), human resource processes (e.g., 360-degree evaluations, exit interviews), employee surveys, focus groups, and interviews. Developing an ethical culture is a continual process that requires constant care and attention.

8.2 Developing an Ethical Culture

The development of an ethical culture depends on how well the organization's mission, values, and standards of conduct align. There is a link between strategic management processes and organizational culture. The strategic management process consists of four phases to achieve corporate goals:

1. The definition of vision, mission, and objectives;
2. Analysis of the internal and external environments;
3. Development of strategies; and
4. Implementation and control of outcomes (Laasch & Conaway, 2015).

Laasch and Conaway (2015) link these strategic processes to responsible companies, stressing the need to include "a vision, mission, and strategic objectives aiming at the creation of a well-balanced triple bottom line of stakeholder value, and moral excellence" (p. 158). For implementation and control, they recommend the balanced scorecard approach developed by Kaplan and Norton (1996), which promotes company objectives that reflect more than financial goals and include learning and growth, internal business processes, and customers.

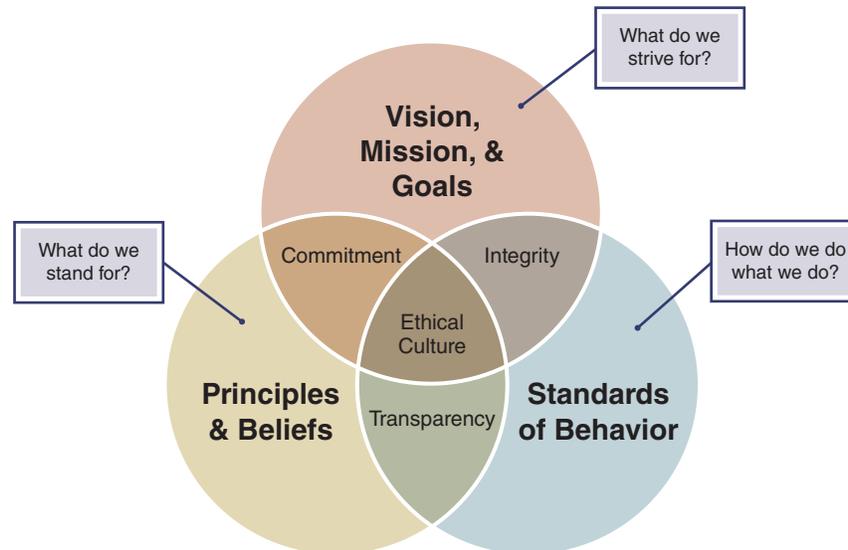
Three Elements of an Ethical Culture

Companies that think strategically can create a culture that can respond to change. David Gebler (2012), a recognized thought leader in the emerging field of values-based ethics and culture risk management, builds on strategic management processes to develop an

integrative model of organizational cultures and values. Figure 8.3 illustrates how the alignment of three elements of culture with values can create an ethical culture.

Figure 8.3: Three elements of an ethical culture

The development of an ethical culture depends on how well the organization’s mission, values, and standards of conduct align.



Source: Modified from Gebler, D. (2012). The 3 power values: How commitment, integrity, and transparency clear the roadblocks to performance. CA: Jossey-Bass.

Each of the elements in Figure 8.3 contributes to developing an ethical culture. The strength of the ethical culture of an organization depends on how well each element aligns. Companies with strong ethical cultures demonstrate a commitment to the organizational purpose and values. A culture of integrity occurs when formal policies align with the mission and goals of the company. A culture of accountability and transparency develops when actions reflect the principles and beliefs of the company. The following sections describe each element individually, but all are equally important to develop an ethical culture.

Vision, Mission, and Goals

The foundation of an organizational culture is the vision, mission, and goals of the company. The **vision statement** expresses the kind of organization the company strives to become. A clear vision is important to lead employees to high performance. Nan S. Russell, author of *The Titleless Leader: How to Get Things Done When You’re Not in Charge* said, “Control the vision, not the process. If you can help others see what you need from them, you’ll be more likely to get it. People want a clear vision of what’s expected so they can successfully achieve it” (Jacobs, 2013). A vision that provides sustained “attention on the essence of winning, motivating people by communicating the value of the target,” demonstrates the strategic intent of the firm (Hamel & Prahalad, 1989, p. 64).

Companies with visions communicating strategic intent gain employee commitment to company goals. Strategic intent denotes the long-term goals of management and reflects core premises about the purpose of the firm in terms of its stakeholders, which leads to greater stakeholder attention (Crilly & Sloan, 2012). A winning focus needs to reflect social, environmental, and ethical responsibilities. An example of a responsible company with strong ethics and responsible management is Ecolab, which espouses the vision statement: “Our vision keeps us focused on what we strive for—to be the global leader in water, hygiene and energy technologies and services; providing and protecting what is vital: clean water, safe food, abundant energy and healthy environments” (Ecolab, 2014, para. 1).

The **mission statement** clarifies the essence of an organization’s existence by defining the organization’s purpose and goals. The vision and mission need to be meaningful and concrete so that employees know how to act accordingly. Articulation of the vision and mission to align with company values is a role of ethical leaders.

Strong leaders are adept at finding the right message and packaging it in a way that is adapted for different groups of employees and other stakeholders so that each can see a link between the vision and their own values and self-concept. This, in turn, should lead to greater commitment toward the vision. (Esper & Boies, 2013, p. 352)

Mary Barra, the CEO of General Motors (GM), recognizes the role of company leadership to build an ethical culture during an interview:

[Culture change] has to be leader-led. Dan (Ammann, GM president) and Mark (Reuss, product development chief) and I have a very strong partnership and a consistency between the three of us, in how we’re conveying to employees what’s important, how we’re going to manage this, and continuing that communication so they feel confident. (Muller, 2014a, para. 13)

Milliman, Gonzalez-Padron, and Ferguson (2012) recommend that companies frame their mission statements in terms of social benefit or purpose to provide greater intrinsic motivation to employees and enhance the organization’s image with external stakeholders. Herman Miller’s mission statement states “Herman Miller strives to create a better world around you—with inspiring designs and inventive services that enhance the places where people work, heal, learn and live, and through its commitment to social responsibility” (Herman Miller, Inc., 2014a, p. 1).

Collins and Porras (1995) describe a visionary company as one that communicates the following three components in a mission statement: (1) core values to which the firm is committed; (2) core purpose of the firm; and (3) visionary goals the firm will pursue to fulfill its mission. **Goals** relate to the company objectives, and include target performance for new market expansion, growth targets, and profits. As shown in Chapter 7, leaders must reinforce that meeting financial goals is an unacceptable rationalization for unethical behavior. A good example is the General Electric (GE) reminders at managerial meetings, such as “No cutting of corners for commercial considerations will be tolerated. Integrity must never be

compromised to make the number” (Heineman, 2008, p. 31). The company’s vision, mission, and goals must align with its values, principles, and beliefs to achieve employee engagement and commitment.

Principles and Beliefs

The principles and beliefs of a company express to stakeholders what the company stands for, and seek to explain why the company is in business. As indicated in Chapter 1, values and principles provide guidelines for employees as they address ethical business issues. Values are an important part of culture, whether it is the culture within an industry or an organization. Core corporate values serve as the cultural cornerstones to guide company conduct (Lencioni, 2002). Not all core values relate to ethical behavior, however, as many businesses stress innovation, performance, and profits. Responsible companies relate their principles to core values, such as integrity, transparency, accountability, and fairness.

As an element of culture, principles and beliefs reflect the norms, or the expected behavior of an organization. As General Motors assesses its culture, consider whether management’s alleged handling of faulty ignition switches aligns with its stated corporate values:

- *Safety and Quality First:* Safety will always be a priority at GM. We continue to emphasize our safety-first culture in our facilities, and as we grow our business in new markets. Our safety philosophy is at the heart of the development of each vehicle. In addition to safety, delivering the highest quality vehicles is a major cornerstone of our promise to our customers. That is why our vehicles go through extreme testing procedures in the lab, on the road and in our production facilities prior to being offered to customers.
- *Create Lifelong Customers:* We take nothing for granted in our efforts to earn the confidence and loyalty of our customers. We listen to customers to make sure we are meeting their needs, and are connecting with them on their terms. Through our relationship with customers, we strive to create passionate brand advocates who love their vehicle and freely tell others about their experience.
- *Innovate:* We challenge ourselves to be creative and lead in everything we do. From implementing the smallest improvements to executing big ideas, we are constantly increasing our competitive advantage to delight and excite our customers.
- *Deliver Long-Term Investment Value:* Our shareholders want to feel confident about their decision to invest in our company. By developing the world’s best vehicles, building upon our strong financial foundation, growing our business, and operating with the highest level of integrity, we will continue to deliver positive results.
- *Make a Positive Difference:* We strive to make a difference in our world and in our workplace. Whether finding new ways to improve our business operations, achieving as part of a team or volunteering in the community, we know that our momentum is tied to positive change. (General Motors, 2014, para. 6)

During Senate testimony, CEO Mary Barra admitted that the culture at General Motors had to change from a cost-cutting culture to a customer-focused culture, stressing the need for all employees to follow correct procedures for safety and quality (Muller, 2014c).

Standards of Behavior

Standards of behavior are a fundamental component of organizational culture. An ethical culture requires that employees have clear expectations of how to handle ethical issues and engage in responsible decision making. Standards include rules, guidelines, policies, and procedures. Yet, having standards of behavior is not enough. Even though Target implemented state of the art data security measures, employees failed to follow procedures when receiving reports of data breaches. A healthy company has standards that align with its mission and values. A good example is expense reporting policies and procedures. Most companies have strict guidelines about gifts and entertainment, tips, and mileage calculations. In spite of these guidelines, company goals to increase sales or satisfy customers may conflict with values of integrity, honesty, and transparency. That may explain why in the United States, fraudulent expense reimbursements often go undetected for up to two years, with more than half of employees failing to report coworkers (Ethics Resource Center, 2013b).

Formal statements that convey the organization's expectations for integrity represent its **code of conduct**. Organizations use a variety of names for ethical standards, such as code of business principles, code of ethics, the way we work, and employee guidelines. Written codes of conduct are an effective tool for guiding employee behavior and are an important part of the formal ethics program of an organization.

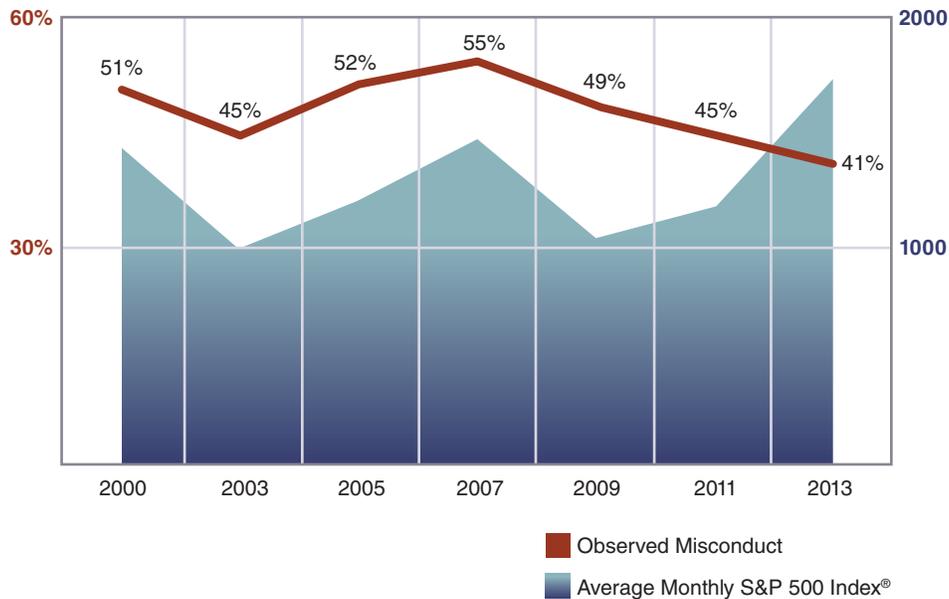
An Ethical Culture During Crises

Economic or financial pressures can increase the willingness to condone unethical practices in the workplace, changing the culture of the organization. The Ethics Resource Center (2013b) has found a tenuous connection between the health of the economy (based on the Standard & Poor's 500 Index) and observed misconduct (see Figure 8.4). The Ethics Resource Center posits that when the economy is doing well, pressure to achieve financial success becomes the primary focus, obscuring awareness of unethical practices. During economic downturns, on the other hand, observed misconduct typically declines.

Historically, the National Business Ethics Survey® observes lower misconduct in times of economic challenge presumably because companies increased their focus on ethics and employees were less likely to endanger employment by breaking the rules. As shown in Figure 8.4, 2013 proved to be an exception to the rule. While the economy improved, there were fewer instances of observed misconduct. The Ethics Resource Center attributes the 2013 reduction in misconduct to greater attention by U.S. companies on developing an ethical culture.

Figure 8.4: Relationship of economy with misconduct

In 2013, observed misconduct declined even as the economy improved.



Source: National Business Ethics Survey of the U.S. Workforce. (2013). Arlington, VA: Ethics Resource Center. Reprinted with permission.

Yet, other examples show how economic pressures lead to greater misconduct. The economic downturn is one reason that Target’s culture moved from a culture of responsiveness and innovation to an organization slow to react to change or crisis. Investigations of the 2010 oil spill in the Gulf of Mexico place much of the blame on a culture of cost cutting at BP plc to make profit targets.

Companies with a healthy ethical culture based on values are more likely to manage economic or financial crises. Karen Doayne, managing director for crisis communication at Burson-Marsteller, stated, “Crisis is a test of character. People will want to know if you lived up to your values” (Ethics Resource Center, 2011, p. 7). See *Business Best: Hartford’s Culture Overcomes Financial Crisis* for an example of a company that recognizes the importance of a healthy organizational culture to meet performance objectives during an economic downturn.

The Hartford found that an ethical culture based on values embedded in principles and standards can enhance an organization’s capacity to overcome an adverse economic environment. Employees perceive that the company consistently follows ethical principles of transparency and accountability. To ensure an ongoing healthy ethical culture, the company should include formal components of an organizational ethical program.

Business Best: Hartford's Culture Overcomes Financial Crisis

The Hartford Financial Services Group, Inc. (known as The Hartford) provides insurance and investment products across the United States. With over 18,000 employees, the company continues to operate since its 1810 inception in Hartford, Connecticut. In 2009, Liam McGee accepted the role of president and CEO of The Hartford in the midst of the financial collapse of 2008, which at the time was threatening the company's existence. The stock price stood at 72% of the 2007 price and the company was facing losses of \$2.7 billion. The company was struggling to honor investment returns and insurance payouts with depleting assets. McGee guided the company through repayment of a \$3.4 billion bailout from the U.S. Troubled Asset Relief Program (TARP), overhauled the company's investment portfolio, and restored the health of the company's balance sheet. The financial turnaround of The Hartford is one of McGee's noted accomplishments during his tenure at the financial services firm.

A shift in the organizational culture allowed The Hartford to recover from the brink of bankruptcy. McGee told a *Forbes* contributor, "During the crisis and even pre-crisis, the company had the opportunity to make the changes it needed to make, but it didn't. People were scared. You had a 200+ year old company that just went through a near-death experience" (Rogers, 2013, para. 5). The company had a culture of silos and individual business unit activity that fostered inertia. The management became risk-averse, relying on extensive discussion and analysis, which ultimately resulted in indecision. McGee created what he calls a "culture of accountability" that required collaboration and transparency. He said, "I expect our leaders to wear two caps—be best at your individual business or function, but also work at what's best for The Hartford," (Rogers, 2013, para. 6).

McGee and newly hired executives from rival insurance firms became role models for a culture of accountability. Under their direction, decisions resulted in action. McGee recounted, "Employees were shocked that we took action, they expected Chris and me to change our minds, to follow the old practice of announcing something and not doing it" (Tully, 2014, para. 14). A focus on accountability and transparency now permeates the company, creating a culture that fosters employee commitment to organizational goals. Eileen Whelley, executive vice president of human resources, said, "We have a culture that is very committed to listening to employees on a regular basis. Our leaders embrace what they hear and take action. Even during the financial crisis, our employees were incredibly loyal because they knew we cared about them and it was clear they care about this company" (Whelley, 2012, p. 49).

Questions to Consider

1. Review The Hartford values and mission at <http://www.thehartford.com>. How do they reflect an ethical culture?
2. In addition to transparency and accountability, what other beliefs and principles contribute to a healthy organizational culture?
3. As a prospective employee considering working for The Hartford, how could you research employee perceptions of the workplace culture?

8.3 Organizational Ethics Programs

An **organizational ethics program** (or business ethics program) is a tool that owners and managers use to inspire, encourage, and support responsible business conduct by designing

structures and systems to guide and support employees and agents. A business ethics program should consider the relevant context of the firm and its organizational culture to identify challenges for behaving appropriately and to develop responsible ways to meet them. An ethics program is part of an organization's compliance initiatives to mitigate risk of illegal conduct. Whatever the size or purpose of the enterprise, owners and managers will find value in building an enterprise that sets standards for responsible business conduct, puts them into practice, and learns from experience. Weber and Wasieleski (2013) find that concern for building an ethical culture is one of the most important motivations for investing in an ethics and compliance program. There is a symbiotic relationship between the organization's ethical culture and formal ethics program. While an ethics program can build an ethical culture, inadequate company attention to the program can weaken the ethical culture, thus rendering the ethics program ineffective.

The Ethics Resource Center (2013b) recommends that an ethics and compliance program include:

- Written standards of ethical workplace conduct;
- Training on the standards;
- Company resources that provide advice about ethical issues;
- A means to report potential violations confidentially, or anonymously;
- Performance evaluations of ethical conduct;
- Systems to discipline violators; and
- A stated set of guiding values or principles. (p. 17)

These criteria relate to those criteria of an effective ethics and compliance program outlined in the U.S. FSGO described in Chapter 4. The following section considers each criterion and how it relates to an ethical culture.

Standards and Procedures

Clear standards and procedures for acceptable behavior are elements of an ethical culture and make up the foundation of an organizational ethics program. To foster an ethical culture, companies need to make clear the organization's expectations for employee behavior. A comprehensive code of ethics sets the bar for the way in which a corporation handles all of its operations. The strength of its ethics code can make the difference between the company's success and failure in avoiding ethical misconduct disasters.

However, policies and procedures can be an overvalued tool in business. Without educating the workforce of the procedures or providing methods of enforcing compliance to the standards and policies, the likelihood for employees to ignore or bypass procedures increases. Companies with business in more than one country have the additional challenge of communicating standards and procedures so that employees worldwide can accept and follow the codes of conduct. The feature *Going Global: IMI plc and Investing in Integrity* describes one multinational company that demonstrates an ethical culture by embedding standards and procedures throughout the business.

Going Global: IMI plc and Investing in Integrity

IMI plc is a global engineering group providing innovative solutions to leading international companies in over 50 countries. Its mission statement is “to become one of the world’s leading engineering companies in the global niche markets we serve and to be recognized for our innovation, application expertise, and global service” (IMI, 2014, para. 2). IMI was the first company to gain the Investing in Integrity Charter Mark across its global business. A charter mark is a common term in the United Kingdom for a **certification mark**, typically a logo or seal that verifies company fulfillment of standards. Ethisphere Institute’s Ethics Inside® Certified logo is another certification of a company’s ethics culture (Ethisphere Institute, 2014).

The Institute of Business Ethics and the Chartered Institute for Securities & Investment developed the Investing in Integrity accreditation system to reassure a company’s key stakeholders that the organization demonstrates a commitment to act with integrity at all times. Companies earning the charter mark demonstrate an ethical culture where ethical policies, procedures, and practices are embedded within the workforce. An important part of the process tests an organization’s commitments to ethics against the employees’ experience of those commitments. Accreditation requires two steps. First, a company completes an online self-assessment of ethical policies, procedures, and practices. Second, an independent assessment, carried out by Investing in Integrity partner GoodCorporation, involves site visits, staff interviews, an employee survey, and reviews of documentation. Upon accreditation, a company may use the charter mark on company material for five years.

The basis of accreditation is an organization’s code of ethics, or similar document, which guides employees on expectations in handling business ethics issues and relationships. Since 2009, IMI has embraced a code of responsible business called “The IMI Way” to reflect its expectations for ethical behaviors. The values of innovation, excellence, and integrity form the foundation for the code. IMI’s code of ethics states:

This code is designed to set a tone and a spirit for us to live by, it is not, and never could be, an exhaustive explanation of the IMI Way. Here we set out our values and standards which help us engage in honest discussions and interactions with our colleagues and other stakeholders such as customers, business partners, communities and investors. (IMI, n.d., p. 3)

Following each standard are examples from employees worldwide who meet the standard, along with instructions on where to find the detailed policies, procedures, and processes that support the standard. Martin Lamb, former CEO of IMI said: “Doing business the right way, the IMI Way, is at the heart of everything we do and we have welcomed the Investing in Integrity initiative as an independent way of verifying that we are meeting, and indeed, exceeding, the high ethical standards we set ourselves across our global organisation” (IMI, 2012, para. 4).

Questions to Consider

1. Why is an organization’s code of conduct the starting point of the Investing in Integrity accreditation?
2. What is the benefit for companies like IMI to seek third party certification of their ethics culture? Consider advantages within and outside the company.
3. How should the accreditor respond should companies have an ethical scandal before the five-year certification expires?

There are no concrete requirements for specific standards and procedures to establish an ethical culture. The code of conduct reflects the unique culture, experiences, and identity of an organization. For example, a company that has unskilled line workers may have to communicate standards in simpler language than a highly technical company does. The code of conduct should focus on specific high-risk issues for the industry and company. Chapter 9 will provide further details for creating an effective code of conduct for an organization.

Program Oversight and Management

The second requirement for an organizational program to contribute to an ethical culture is program oversight and management, which ensure adequate attention to the formal and informal ethical culture from senior management and the board of directors. As introduced in Chapter 1, top management commitment to stressing ethical programs is the most important component in encouraging ethical behavior and creating an ethical culture in an organization. Chapter 7 stressed the role of ethical leaders in creating an ethical culture. Many companies establish departments solely to manage the ethics program, led by a chief ethics officer, chief compliance officer, or similar title. Ethics and compliance professionals contribute to building trust among employees and external stakeholders that the company will act with integrity. In the United States, the board of directors has a legal obligation to oversee the ethics and compliance of an organization. The 2004 and 2010 amendments of the FSGO encourage companies to allow the chief ethics and compliance officer access to the board of directors.

How can a smaller organization provide program oversight and management? As mentioned earlier, ethical cultures develop differently in smaller, family-owned companies than in large publicly listed corporations. Ethical values are connected to the founder's values, and management of ethical issues occurs on a more individualized basis. However, small and medium enterprises may not have the resources of a larger company to invest in an organizational ethics program. Rather than having a CEO represent top management commitment, the owner-manager of a small company sets the tone at the top. A smaller organization is unlikely to hire a dedicated ethics professional since its employees are typically generalists with flexible and multiple roles. Chapter 9 will explore methods for both large and small companies to establish effective program oversight and management.

Vetting the Delegation of Substantial Authority

In line with the requirement for program oversight and management, the FSGO also have a requirement for investigating individuals in the company with substantial authority. The definition of **substantial authority personnel** is broad and can include many members of the management team. The guidelines stipulate:

“Substantial authority personnel” means individuals who within the scope of their authority exercise a substantial measure of discretion in acting on behalf of an organization. The term includes high-level personnel of the organization,

individuals who exercise substantial supervisory authority (e.g., a plant manager, a sales manager), and any other individuals who, although not a part of an organization's management, nevertheless exercise substantial discretion when acting within the scope of their authority (e.g., an individual with authority in an organization to negotiate or set price levels or an individual authorized to negotiate or approve significant contracts). Whether an individual falls within this category must be determined on a case-by-case basis. (United States Sentencing Commission, 2013, p. 492)

The definition of substantial authority posed by the United States Sentencing Commission recognizes that top managers and executives are not the only perpetrators of occupational misconduct. One study found that individuals in purchasing and procurement or marketing functions are most likely to be involved in and vulnerable to white-collar crime (Gottschalk, 2011). The Association of Certified Fraud Examiners (2012) reported that over two thirds of occupational fraud is instigated by individuals working in accounting, operations, sales, executive/upper management, customer service, and purchasing. Companies can incur fines and penalties for misconduct perpetrated by just a few employees or consultants, such as Alcoa's fines for the overseas manager and independent consultant who bribed Bahraini officials to secure business with a government-owned aluminum plant (ElBoghdady, 2014). Banks involved in an interest manipulation scandal claimed that a small number of individual employees committed the unethical practices in violation of company values and policies (Mock & Enrich, 2013).

The FSGO stipulate that an effective organizational ethics program should "use reasonable efforts not to include within the substantial authority personnel of the organization any individual whom the organization knew, or should have known through the exercise of due diligence, has engaged in illegal activities" (United States Sentencing Commission, 2013, p. 498). Reasonable efforts include background checks, interviews, and personality assessments. Through a comprehensive pre-hire screening of managers and employees that engage in high-risk business decisions, companies can avoid hiring individuals with predispositions to misconduct and seek employees who fit into an ethical culture.

To maintain an ethical culture, organizations should periodically conduct reviews of individuals with substantial authority to detect symptoms of misconduct. According to the Association of Certified Fraud Examiners (2012), individuals with past employment or legal problems were a small percentage of the perpetrators of occupational fraud. Table 8.2 provides a summary of behavioral red flags associated with misconduct by profession. Overall, the most common warning signs were living beyond their means (36% of cases), financial difficulties (27%), unusually close association with vendors or customers (19%), and excessive control issues in sharing duties (18%). Addiction to alcohol and drugs remains a problem for organizations, leading to regular drug testing for all positions. However, testing for controlled substances can decrease employee commitment when not implemented fairly (Konovsky & Cropanzano, 1991).

Table 8.2: Behavioral red flags by profession

Profession Behavioral Red Flag	Executive/ Upper Mgmt.	Accounting	Operations	Sales	Purchasing	Customer Service
Living Beyond Means	48.1%	43.7%	31.9%	25.9%	38.2%	35.9%
Control Issues	26.4%	19.5%	21.1%	11.8%	22.4%	4.3%
Financial Difficulties	25.2%	30.4%	31.5%	27.1%	15.8%	33.7%
Unusually Close Associations	22.6%	6.1%	28.9%	18.2%	47.4%	12%
Divorce/Family Problems	13.8%	18.8%	15.9%	12.4%	9.2%	17.4%
Past Employment-Related Problems	11.9%	6.5%	9.5%	9.4%	3.9%	7.6%
Addiction Problems	10.7%	11.3%	7.8%	4.7%	6.6%	8.7%
Past Legal Problems	8.2%	5.8%	4.3%	3.5%	1.3%	6.5%

Source: Association of Certified Fraud Examiners. (2012). *Report to the nations on occupational fraud and abuse: 2012 global fraud study*. Austin, TX: Association of Certified Fraud Examiners, Inc.

Removing individuals prone to misconduct in order to maintain an ethical organization is reflective of the bad apple theory, which posits that corporate crime is the result of one individual who is inherently immoral, greedy, or manipulative (Treviño & Brown, 2004). News coverage of company scandals include visuals of executives handcuffed and escorted to a waiting police vehicle. The “perp walks” of the arrests of Bernie Madoff, Ken Lay, and Goldman Sachs trader Fabrice Tourre promulgate the bad apple theory. However, this theory fails to account for the systematic breakdowns that typically contribute to misconduct. As Treviño and Brown (2004) stress, most employees are followers and much “unethical behavior in business is supported by the context in which it occurs—either through direct reinforcement of unethical behavior or through benign neglect” (p. 72). Therefore, an ethical culture supported by an organizational ethics program can guide employees on how to address ethical business issues.

Training and Communication

Training and communication are important elements of embedding ethical standards throughout an organization. The FSGO stipulate that “The organization shall take reasonable steps to communicate periodically and in a practical manner its standards and procedures . . . by

conducting effective training programs and otherwise disseminating information appropriate to such individuals' respective roles and responsibilities" (United States Sentencing Commission, 2013, p. 498). This requirement stresses that an ethical culture requires both training and communication.

Though research supports that ethics training reduces pressure to compromise ethical standards and increases the likelihood that employees will report misconduct, awareness of ethics training varies worldwide. A 2012 study of employees in Italy, France, Germany, and Spain found that overall, less than half of companies based in those countries provide ethics training, ranging from 23% in Germany and 27% in France, to 47% in Spain and 60% in Italy (Basran, 2012). In England, on the other hand, almost two thirds (68%) of full-time employees in the 2012 British Ethics at Work Survey said their organization provides ethics training (Basran & Webley, 2012). One explanation for the lower prevalence of ethics training in France and Germany is that although ethics programs are in place, the companies are not effectively communicating the training throughout the organization. Over 20% of the employees in continental Europe were not able to answer affirmatively to the question "My organisation provides training on standards of ethical conduct," while 27% of German employees were unsure if ethics training exists in their organization (Basran, 2012). In contrast, only 4% of British respondents indicated not knowing if their organization offered ethics training (Basran & Webley, 2012). In the United States, the percentage of companies providing ethics training rose from 74% in 2011 to 81% in 2013 (Ethics Resource Center, 2013b).

Open communication and relevant ethics training encourages an ethical culture. Communication barriers among departments are one explanation for the lapse of safety protocols at GM and risky investments at The Hartford (Muller, 2014c; Tully, 2014). In contrast, leadership at the chemical company, Ecolab, explicitly emphasizes the importance of cross-departmental communication and cooperation among employees (Milliman et al., 2012). Ethics training should be relevant to the audience, yet consistent with the organization's values, principles, and ethical standards. Not all employees need to be aware of every policy and procedure in the company. Rather, employees need training on the specific risks that could arise in their work and sources for assistance in resolving ethical dilemmas. Chapter 9 will provide methods for educating the workforce on company ethical standards and program elements.

Checking, Evaluating, and Reporting

An indication of an ethical culture is the degree to which employees are comfortable in reporting misconduct without fear of retaliation. Employees become reluctant to share bad news if the company culture reprimands employees for reporting misconduct. Earlier in the chapter, rationale for measuring the strength of the company's ethical culture included exploring employee perceptions of acceptable behavior. In recognition of the need for continuous monitoring of the ethical climate of an organization, the FSGO recommend that organizations take the following steps:

1. To ensure that the organization's compliance and ethics program is followed, including monitoring and auditing to detect criminal conduct;

2. To evaluate periodically the effectiveness of the organization's compliance and ethics program; and
3. To have and publicize a system, which may include mechanisms that allow for anonymity or confidentiality, whereby the organization's employees and agents may report or seek guidance regarding potential or actual criminal conduct without fear of retaliation. (United States Sentencing Commission, 2013, p. 498)

The criteria for evaluating an organizational ethics program require an organization to pose three questions about its ethical culture. First, are there controls in place to detect deviance from company policies and procedures? Second, is the organization acting according to its ethical standards? Lastly, are employees comfortable speaking up about potential or observed misconduct?

A strong ethical culture will demonstrate a commitment to ethical conduct by implementing controls such as periodic audits, approval processes, and documentation requirements. Employees perceive that the company cares about maintaining ethical standards when everyone must abide by the same rules. In Senate hearings, when asked why an engineer redesigned a defective ignition switch without properly recording the procedure, GM's CEO Mary Barra had to answer accusations of what one senator called a "culture of cover-up" (Muller, 2014c, para. 2). Barra stated in a 2014 *Forbes* interview that the company is addressing a "culture of fear" within GM, a fear of rocking the boat, by implementing a Speak Up For Safety program. She said:

If someone picks up the phone and says, "Hey, I'm worried about x, y or z," it's important that you answer them, either to say, "Wow, thank you for raising that issue," or "Hey, that's not an issue and here's why," so they don't leave thinking, "I tried, and they didn't listen to me. They just ignored me." (Muller, 2014a, para. 15)

Recall the challenges in assessing the strength of an ethical culture presented earlier in the chapter. Meaningful metrics of the ethical culture should take into account the organizational characteristics and industry environment. The metrics need to be quantifiable to evaluate improvements in the ethical culture or identify risks for misconduct. A common metric is the number of misconduct reports made to the company ethics department. The challenge with that metric is interpreting variations in the number of reports. If reports of misconduct increase, it could signify that employees are more effective at identifying ethical issues than they were in months or years past. Alternatively, increased misconduct reports may simply reflect that employees have become more willing to report. Both reasons could indicate an effective ethics program. On the other hand, increased observations of misconduct may also signal a weakening of the ethical culture—that more employees are ignoring ethical standards.

Lockheed Martin was able to show that a significant difference in the number and nature of calls to their ethics department reflected a successful implementation of its new ethics training program (Gonzalez-Padron, Ferrell, Ferrell, & Smith, 2012). Ethics officers were handling more calls for guidance rather than reporting. During the calls, officers reinforced the vocabulary and a technique from the training to encourage resolution before an ethical problem escalated. Options for encouraging employees to report misconduct and assessing the ethics program are presented in Chapter 9.

Disciplinary Procedures and Incentives

Employee perceptions of fairness and an organization's consistency in enforcing policies and procedures are an important part of establishing an ethical culture. Discipline for rule violators sends a strong message to employees: it "reinforces standards, upholds the value of conformity to shared norms, and maintains the perception that the organization is a just place where wrongdoers are held accountable for their actions" (Treviño et al., 1999, p. 139). To assess whether employees perceive that the organization enforces policies and procedures, Cullen and Victor (1993) suggest asking employees to rate the truth of four statements:

- It is very important to strictly follow the company's rules and procedures.
- Everyone is expected to stick by company rules and procedures.
- Successful people in this company go by the book.
- Successful people in this company strictly obey the company policies.

Recognizing that consistent enforcement of ethical standards influences the ethical culture of an organization, the FSGO includes the following criterion:

The organization's compliance and ethics program shall be promoted and enforced consistently throughout the organization through (A) appropriate incentives to perform in accordance with the compliance and ethics program; and (B) appropriate disciplinary measures for engaging in criminal conduct and for failing to take reasonable steps to prevent or detect criminal conduct. (United States Sentencing Commission, 2013, p. 498)

The original language of the FSGO stressed discipline of misconduct over incentives for ethical behavior. Despite this emphasis, programs rewarding individuals who demonstrate exemplary performance in upholding ethical standards are emerging as more companies recognize that monetary incentives affect the ethical behaviors of employees (Chen & Sandino, 2012; Tenbrunsel, 1998). The Swiss-based pharmaceutical company Novartis International AG bases salary and bonus increases, in part, on evaluations of employee behavior that aligns with company values (Basran & Webley, 2012). Employees at Novartis must meet business objectives and behave ethically in order to receive the greatest compensation.

Other company incentives for demonstrating ethical behaviors can include employee recognition awards, either through a company selection process or by peers. A St. Louis-based construction services company, ADB Companies, Inc. encourages field management or employees to award a Spot Award for a fellow worker working safely (ADB, 2013). Each Spot Award winner receives a gift card and recognition in the company newsletter. Companies like Novartis and ADB recognize that employees pay attention to how leadership responds to violations and rewards ethical behavior.

Response to Critical Issues

In order to establish an effective ethics and compliance program, organizations must respond appropriately to critical issues. In doing so, they must investigate, remediate, and disclose reports of misconduct. This step builds on the previous two steps—monitoring and encouraging reporting of misconduct, and consistent enforcement of standards. Establishing and

communicating clear guidelines for the investigation of ethics and compliance issues ensures predictability, consistency, and confidence in the process. The FSGO stipulate “After criminal conduct has been detected, the organization shall take reasonable steps to respond appropriately to the criminal conduct and to prevent further similar criminal conduct, including making any necessary modifications to the organization’s compliance and ethics program” (United States Sentencing Commission, 2013, p. 498).

Once aware of misconduct, a company must determine if the action is subject to criminal prosecution. Most investigations focus on unethical behavior inconsistent with the company code of conduct and do not require legal action (Ethics & Compliance Officer Association Foundation, 2008). If the action requires prosecution, the company should then inform the appropriate governmental authority prior to commencement of regulatory investigations. Failure to do so may result in fines and penalties.

Investigations of misconduct create tensions among employees or between management and employees that can weaken an ethical culture. The FSGO do not dictate that an internal investigation process should exist, however, companies find that handling misconduct internally before the situation escalates can mitigate risk of illegal behavior. *The Ethics and Compliance Handbook* provides guiding principles to respond to reports of misconduct:

- An organization must conduct a prompt, effective, and thorough investigation when it receives an allegation of unethical or illegal behavior.
- The purpose of an investigation is to establish . . . exactly what happened and what the organization can learn about preventing future misconduct; determining the consequences to the individuals involved should be handled separately.
- Each person who is the focus of an investigation . . . must be treated with respect and dignity. . . .
- . . . An organization may well decide as a matter of fairness or good business practice to presume that someone accused of acting illegally, unethically, or in violation of organization policy is innocent until proven otherwise.
- Confidentiality of investigations should be maintained to the greatest extent possible.
- The organization must proactively work to prevent retaliation against employees who allege misconduct in good faith. (Ethics & Compliance Officer Association Foundation, 2008, p. 98)

Heinz states in its code of conduct that employees who report a violation in good faith will not be subject to retaliation. However, the company cautions that “A violation of the requirement to report violations or to cooperate in an investigation may result in disciplinary action” (Heinz, 2010, p. 8). United Technologies Corporation uses ombudsmen as neutral liaisons between the employee and the company in receiving reports of misconduct (LRN, 2007a). Chapter 9 will provide specific guidelines for conducting investigations of reported misconduct.

Periodic Risk Assessment

The final criterion for an organizational ethics program involves conducting periodic risk assessments. **Risk** is “the possibility that an event will occur and adversely affect the achievement objectives” (The Committee of Sponsoring Organizations of the Treadway Commission,

2013, p. 4). **Risk assessment** refers to a systematic process for identifying and evaluating events that could affect the achievement of company objectives. Risk assessment is the basis for **enterprise risk management**, defined as “the process of aligning competitive strategy with the mechanisms that identify, aggregate, mitigate, avoid, and transfer risk” (LRN, 2007a, p. 2).

Identifying risk is part of the business strategic management processes of business planning through analysis of the internal and external environments. The FSGO recommend that a company “periodically assess the risk of criminal conduct” and take appropriate action to modify the organizational ethics program if necessary (United States Sentencing Commission, 2013, p. 498). Defining ethics and compliance risk is a necessary task for building an ethical culture. The Committee of Sponsoring Organizations of the Treadway Commission’s framework for internal controls mentioned in Chapters 1 and 4 considers risk assessment a part of the process to provide assurance of compliance to laws and regulations

A periodic risk assessment can provide valuable information for maintaining an ethical culture, such as evaluating the effectiveness of the company’s ethics and compliance program. Regular review of the internal and external environments allows an organization to accommodate changes in the legal and regulatory landscape as well as business and organizational changes such as mergers or new business models. The risk assessment should prioritize risks according to their likelihood of occurrence and seriousness of impact; and include an evaluation of why the risks occur and how to reduce each. The result is an action plan to mitigate high-priority risks. The detailed steps to conduct a risk assessment are explored in Chapter 9.

Summary & Resources

Chapter Summary

Culture matters in business. The culture of an organization consists of shared basic values, behavioral norms, and visible artifacts that guide appropriate behaviors and ethical decision making. A healthy culture allows employees to live their values and perform without fear of retaliation; whereas dysfunctional cultures lead to poor decisions, lower performance, and greater risk of ethical misconduct scandals.

A main driver for investing in an ethical organizational culture is to comply with national guidelines and regulations such as the FSGO. In addition, the ethical culture of an organization can incentivize employees’ behaviors, align the informal culture of the organization with the formal policies and procedures, and attract and retain a talented workforce. The creation of an ethical culture depends on how well the organization’s mission, values, and standards of conduct align. The vision and mission statement need to be meaningful and concrete so that employees know how to act accordingly. Articulation of the vision and mission to align with company values is an important role of ethical leaders. In developing an ethical culture, organizations should consider how the national economy could influence employee alignment with organizational values and commitment to ethical standards.

An organizational ethics program is part of the formal ethical culture. The goal is to inspire, encourage, and support responsible business conduct through structures and systems that guide and support employees and agents. There is a symbiotic relationship between the organization’s ethical culture and formal ethics program. While an ethics program can build an ethical culture, inadequate company attention to the program can weaken the ethical culture,

thereby rendering the ethics program ineffective. An ethics and compliance program must meet the following requirements as established by the FSGO: 1) standards and procedures, 2) program oversight and management, 3) delegation of substantial authority, 4) training and communication, 5) checking evaluation and reporting, 6) consistent disciplinary procedures and incentives, 7) response to critical issues, and 8) periodic risk assessment.

Key Terms

artifacts Tangible visible or audible expressions of the shared values and norms of an organization.

certification mark A logo or seal that verifies company fulfillment of standards.

code of conduct Formal statements that convey the organization's expectations for integrity and become an effective tool for guiding employee behavior.

enterprise risk management The process of aligning competitive strategy with the mechanisms that identify, aggregate, mitigate, avoid, and transfer risk.

ethical climate The shared perception of what constitutes ethically appropriately behavior and knowledge of procedural steps to address an ethical issue.

goals The objectives a company is striving to achieve, including target performance for new market expansion, growth targets, and profits.

mission statement A written statement that clarifies the essence of an organization's existence by defining the organization's purpose and goals.

moral misalignment Ethical or moral differences in how the company and an employee believes the firm should operate.

norms Expectations of desirable behavior found in the policies and procedures that guide organizational decisions and actions.

organizational culture The pattern of shared values and beliefs that helps individuals understand organizational functioning and thus provides them with the norms for behavior in the organization.

organizational ethics program A tool that owners and managers use to inspire, encourage, and support responsible business conduct by designing structures and systems to guide and support employees and agents.

risk The possibility that an event will occur and adversely affect the achievement objectives.

risk assessment A systematic process for identifying and evaluating events that could affect the achievement of company objectives.

shared basic values Basic assumptions outlining desirable ends and means that a group has invented, discovered, or developed, and that have worked well enough to be considered valid, and, therefore, to be taught to new members.

substantial authority personnel Individuals who, within the scope of their authority, exercise a substantial measure of discretion in acting on behalf of an organization.

vision statement Written narrative that delineates what an organization ultimately should become and achieve.

Critical Thinking and Discussion Questions

1. What is the difference between the ethical culture and the ethical climate of a company? How are they interrelated?
2. How would you convince an organization to invest in an ethical culture? Develop a proposal for management to develop an ethical culture.
3. Assess the ethical culture of an organization where you currently work or would like to work. Consider how to discern the values, norms, and artifacts of the organization.
4. Review Ethisphere Institute's most recent list of the World's Most Ethical Companies. Which companies do you recognize? What companies are not there that you would expect to see? Review some of the listed companies' websites to see if the Ethisphere certified label appears.
5. Look up the vision and mission statement of a company of your choice and rewrite it by integrating responsible business considerations. Then rewrite the strategic goals based on the new mission statement.
6. How can an organizational ethics program be effective in guiding the informal culture to support ethical behaviors? Argue for an organizational ethics program as part of an ethical culture.
7. Relate the criteria for an organizational ethics program to the elements of an ethical culture in Figure 8.3.

Suggested Resources

Investing in Integrity

<http://www.investinginintegrity.org.uk>

Institute of Business Ethics

<http://www.ibe.org.uk>

GoodCorporation

<http://www.goodcorporation.com>

Ethics Resource Center

<http://www.ethics.org>