

Maintaining and Developing Ethical Corporate Culture

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Abstract

Of all the issues boards of directors, executives, and managers face, one could argue that unethical corporate activity is one of the most significant in terms of its potential negative impact and also one of the most difficult to properly address. This article argues that three key elements must exist if illegal or unethical activity within and on behalf of organizations is to be minimized through developing and sustaining an ethical corporate culture. The three elements include (1) the existence of a set of core ethical values infused throughout the organization in its policies, processes, and practices; (2) the establishment of a formal ethics program, including a code of ethics, ethics training, an ethics hotline, and an ethics officer; and (3) the continuous presence of ethical leadership—that is, an appropriate ‘tone at the top’ as reflected by the board of directors, senior executives, and managers. While each of these three elements is distinct, they also overlap, relate to, and reinforce each other. This article discusses each of the three key elements necessary to develop and maintain an ethical corporate culture

Keywords: *Ethical corporate culture; Ethical values; Ethics programs; Ethical leadership.*

Unethical Corporate Activity

It can be argued that of all the issues faced by boards of directors, executives, and managers, unethical corporate activity is one of the most significant in terms of its potential negative impact and one of the most difficult to properly address. The range of illegal and unethical activity taking place is extensive and includes corruption, bribery, receiving and giving gifts and entertainment, kickbacks, extortion, nepotism, favoritism, money laundering, improper use of insider information, use of intermediaries, conflicts of interest, fraud, aggressive accounting, discrimination, sexual harassment, workplace safety, consumer product safety, and environmental pollution [1]. Unfortunately, one does not have to look very far to see significant examples of crime and unethical activity within or on behalf of business organizations and the serious negative impacts such scandals have had on

investors, employees, customers, competitors, the natural environment, and society (e.g., Enron, World Com, Tyco, Parmalat, Siemens, Madoff Investments, BP).

This list does not include the more basic legal yet unethical practices by firms and their agents, including acts of dishonesty, disloyalty, disrespect, or promise breaking, all of which can also result in unnecessary harm to stakeholders. However, beyond the major scandals that are often the focus of media scrutiny, lawsuits or government prosecutions are the more difficult and challenging ethical dilemmas managers face. For example, consider the following firm-level ethical dilemmas with which many managers must wrestle:

- Should production be moved overseas, leading to worker layoffs?

- Should affirmative action policies be adhered to, leading to other qualified candidates being bypassed?
- Should consumer products be sold in third world countries with less stringent consumer protection laws when their sale would not be legally permitted in the firm's home country?
- Or consider the following individual-level ethical dilemmas managers might face:
- Should I break confidentiality and indicate to a work colleague who is also a good friend that he/ she is about to be laid off?
- Should I accept an expensive bottle of wine during the holiday season from a current supplier if the firm does not forbid this?
- Should I join my work colleagues when a potential client is being taken to an adult entertainment club?
- Should I report my supervisor who is acting in an abusive manner toward other employees and thereby risk losing my own job?

How can firms prevent significant unethical behavior while simultaneously providing proper guidance to managers and employees in how to address more challenging day-to-day ethical dilemmas? While a vast array of potential solutions has been presented, many theorists [2] argue that the presence of an ethical corporate culture is a necessary, although insufficient, condition if the extent to which illegal or unethical activity is taking place is to be minimized. An ethical corporate culture not only helps avoid major illegal or unethical corporate scandals but also leads to more appropriate ethical behavior at all firm levels.

This theoretical position is at least initially supported by empirical evidence. For example, the 2009 National Business Ethics Survey of 2,852 U.S. employees conducted by the Ethics Resource Center [3] found that in stronger ethical cultures, far fewer employees feel pressure to commit misconduct (4% versus 15%), the rates of observed misconduct are much lower (39% versus 76%), employees who observe misconduct are more likely to report it (43% versus 28%), and those who report misconduct are less likely to experience retaliation (4% versus 24%). In reviewing the academic literature, McDonald [4] suggests: "The results highlight the

important role that organisational culture plays in ethical decision making. However, there are several difficulties with an approach focusing on developing an ethical corporate culture to help combat illegal or unethical activity. The initial challenge lies in understanding what exactly defines an ethical corporate culture.

Before this can be done, however, one must start with defining the broader corporate culture concept found in the organizational theory literature. While several definitions exist, for the purposes of this article, corporate culture is simply considered a representation of the organization's shared assumptions, values, and beliefs. Building on this general definition, Treviño and Nelson [5] suggest that an ethical corporate culture represents a slice or subset of the organization's broader culture and is "maintained through a complex interplay [and alignment] of formal [i.e., policies, leadership, authority structures, reward systems, training programs] and informal organizational systems [i.e., peer behavior and ethical norms]."

In terms of how an ethical corporate culture can lead to expected ethical behavior, employees can act in accordance with the firm's ethical norms either through a socialization process (i.e., employees feel they are expected to behave accordingly) or an internalization process (i.e., employees adopt the ethical norms as their own). The goal, then, is for firms to ensure that within their broader corporate culture of shared values and beliefs, a strong ethical corporate culture also exists rather than a weak culture. Only when this takes place will employees be more likely to conform to desired ethical norms.

A second difficulty lies in asking whether its existence-however defined-will actually make a difference with respect to all employees and managers. For the purposes of this article, this position is rejected as being clearly unrealistic as illegal and unethical activity will always continue, despite the existence of even an ideal ethical corporate culture. For example, there are many individuals in the fraud-prevention field who accept a 20-60-20 rule.

Namely, 20% of a given workforce will always do the right thing; that is, act legally or ethically regardless of one's circumstances or work environment. Another 20% will always engage in illegal or unethical behavior when the opportunity exists, the rewards are sufficient, and there is a perceived low likelihood of getting caught. The remaining 60% of the workforce, while basically honest, will decide to engage in illegal or unethical behavior depending on the environment in which they work and factors like managerial pressure, peer pressure, or reward systems or the belief that they are acting in the firm's best interests. Such employees can be referred to as 'fence sitters.' Turning this fact into a potential opportunity, it is this 60% that can arguably be most influenced to do the right thing when they work within an ethical corporate culture. Consequently, these fence sitters are the target group of this article. The goal is to identify measures that can help mitigate or minimize - as opposed to completely eliminate - the extent to which illegal or unethical activity takes place within or on behalf of businesses.

However, even among fence sitters, an additional preliminary hurdle remains. Are employees who can be socialized to act in an ethically appropriate manner even able to initially recognize that they are in the midst of an ethical dilemma? For example, one study found that when asked to describe a moral dilemma they had experienced, two-thirds of 18 to 23-year-olds were "unable to answer the question or described problems that are not moral at all, like whether they could afford to rent a certain apartment or whether they had enough quarters to feed the meter at a parking spot" [6].

When this additional ethical awareness hurdle is added, those who would normally act ethically or those who can be socialized to act ethically may not do so because they may not recognize they are facing an ethical dilemma. The actual distribution of those employees who would always act ethically, might act ethically, or never act ethically when lack of ethical awareness is also taken into account, would actually approximate something closer to 10-50-40 rather than 20-60-20. Regardless of the actual distribution, it becomes extremely important for board

members, executives, and managers to understand how to best develop and sustain an ethical corporate culture with respect to employees who can be sensitized to become aware they are facing ethical dilemmas or employees who can be influenced by their work environments. While recognizing there is no one-size-fits-all solution for all business organizations, one can certainly postulate that certain core elements should be in place to have the greatest chance of developing and maintaining an ethical corporate culture.

A key question then arises: What critical elements are necessary to develop and sustain an ethical corporate culture? Based on a review of the extant literature, this article argues that three key elements must necessarily exist if crime, corruption, and other illegal or unethical activity within and on behalf of businesses are to be minimized through building an ethical corporate culture:

- A set of core ethical values infused throughout the organization in its policies, processes, and practices;
- A formal ethics program, including a code of ethics, ethics training, an ethics hotline, and an ethics officer;
- The continuous presence of ethical leadership (i.e., an appropriate tone at the top as reflected by the board of directors, senior executives, and managers).

While these three elements are distinct, they also overlap, relate to, and reinforce each other. As part of an effort to consolidate the extensive theoretical and empirical business ethics research that has been conducted to date, each of the three key elements necessary to develop and maintain an ethical corporate culture will now be discussed.

First Pillar: Core Ethical Values

A set of core ethical values appears to be critical in establishing an ethical corporate culture. As articulated by Hunt, Wood, and Chonko [7], "corporate values have long been referred to as the central dimension of an organization's culture." An ethical corporate culture has, in turn, been recognized as important to ethical decision making. Indeed, O'Fallon and Butterfield [8]

state that “research generally supports the notion that ethical climates and cultures have a positive influence on ethical decision making.” Despite the recognized importance of core ethical values, however, research likewise suggests that many employees perceive their firms to be lacking ethical values. For example, of 23,000 U.S. employees surveyed, only 15% felt they worked in a high-trust environment, only 13% had highly cooperative working

relationships with other groups or departments, and only 10% felt their organization holds people accountable for results [9].

Although there are a number of potential ethical values from which a firm may choose, it could be argued that one needs to attempt to identify those ethical values that can be considered universal in nature.

Table 1: Ethical dilemmas and potential application of ethical values

Ethical Dilemma	Application of Ethical Values
Should I break confidentiality and indicate to a friend that he/she is about to be laid off?	While values like loyalty to one's friend or caring (i.e., trying to avoid unnecessary harm) suggest breaching confidentiality and disclosing the information to one's friend, other aspects of trustworthiness (e.g., loyalty to the firm, honesty, and promise keeping) suggest maintaining confidentiality despite pressure to do otherwise.
Do I accept an expensive bottle of wine during the holiday season from a current supplier if the firm does not forbid this?	While one might argue that accepting gifts is the norm and there is no current apparent conflict of interest, the ethical values of fairness (e.g., perceived conflict of interest) and loyalty to the firm and its owners suggest otherwise. At a minimum, if refusing the bottle of wine would be problematic, then the gift should become the property of the firm rather than the property of the individual receiving the gift.
Do I fully disclose a mistake made to a client or customer when they will not notice and the mistake is significant?	This issue can place potential negative financial considerations of losing the client into conflict with ethical values. The core values of trustworthiness (i.e., loyalty, honesty, promise keeping, integrity) clearly suggest that disclosure must take place. Respect for the client suggests that disclosure should take place. Responsibility also suggests that accountability for the mistake should be taken, and fairness would require compensation to be provided if the mistake caused any loss to the client/customer.

To the greatest extent possible, the selected moral values should retain their significance despite differences in culture, religion, time, and circumstance. A large number of diverse individuals and social groups should view the values as being fundamentally important in guiding or evaluating behavior, actions, or policies. Along these lines, universal moral values are considered to be similar to hypernorms, which Donaldson and Dunfee [10] describe as “deep moral values” representing “a convergence of religious, political, and philosophical thought”. Hypernorms are considered “so fundamental that, by definition, they serve to evaluate lower-order norms [while]... reaching to the root of what is ethical for humanity”. One list that has been proposed suggests the following set of universal core ethical values for all business firms [11]:

- Trustworthiness, including honesty, promise keeping, integrity, transparency, reliability, and loyalty;
- Respect, including respect for human rights;
- Responsibility, including accountability, accepting fault, and not blaming others;

- Fairness, including notions of process, impartiality, and equity;
- Caring, including sensitivity toward others and avoiding unnecessary harm;
- Citizenship, including obeying laws, assisting the community, and protecting the environment.

Can the application of such core ethical values actually assist managers and employees in determining the appropriate course of ethical conduct? To help illustrate their potential, Table 1 provides a brief analysis of how several of the aforementioned core ethical values can be applied to resolve typical ethical dilemmas faced in the workplace.

If applied to business practices, core ethical values can sometimes constrain the firm's self-interest; however, in other cases, consistently applying such values helps ensure the long-term financial prosperity of the firm. Regardless of whether applying ethical values always leads to profit maximization, it can be argued that all business firms should attempt to infuse core ethical values throughout their organizations

as the basic starting point for establishing an ethical corporate culture. This infusion should take place within the firm's (1) policies, (2) processes, and (3) practices.

Policies

First, whenever possible, core ethical values must be made explicit in the firm's policy documents. The most important document in which values should be present is the firm's code of ethics, and they should be stated up-front. Values should also be included in the firm's annual report, public accountability statement, or social report, and they should be indicated as clearly as possible on the homepage of the firm's website. Although being explicit about ethical values might expose a firm to additional critique from academics, the media, non-governmental organizations (NGOs), customers, and even employees, this should be considered a necessary step toward establishing an ethical corporate culture.

Of course, even firms like Enron - despite being quite explicit in its office banners and training videos about the company's core ethical values, including integrity, honesty, and respect - failed to live up to them. This makes it clear that values must be incorporated into other processes and practices, too.

Processes

Values only become alive and lead to a more ethical corporate culture when they are infused and observed throughout the firm's processes. The first process involves hiring; namely, the right people need to be recruited. There are various methods that can be used to build ethical values (e.g., honesty, integrity) into the hiring process, such as testing and interviews. Certain questions (e.g., "Have you ever faced an ethical dilemma before? If so, how did you handle it?") have the potential to reveal an applicant's general awareness of ethical issues and his/her perspective on ethical decision making. Certain answers (e.g., "I don't think I've ever faced an ethical dilemma") suggest a lack of awareness and might represent a red flag during the hiring process. Hiring ethical leaders at the more senior levels can be critical if an ethical tone at the top is to be established. While concerns have been raised over the use and effectiveness of integrity testing, this tool

also remains an important measure for employers to screen out 'executive psychopaths,' who-despite their polish, charm, and cool decisiveness-are "cunning, manipulative, untrustworthy, unethical, parasitic, and utterly remorseless," thus making them dangerous to their companies [12]. Ethical values should be considered the filter or gate through which potential new employees or managers must pass before financial performance factors may even be considered when hiring. Firms might ponder utilizing a group decision-making approach when hiring at the senior levels (as opposed to one-on-one hiring interviews only) as this process better facilitates raising ethical red flags regarding candidates.

Ethical values should also be part of any orientation process, such as ethics training. Performance appraisals should also consider employees' behavior with respect to ethical values: "An effective performance management system is a key component of the ethical culture. The system plays an essential role in alignment or misalignment of the ethical culture because people pay attention to what is measured, rewarded, and disciplined" [5]. While it is sometimes more difficult in a performance appraisal to measure behavior that conforms to ethical values, it is easier to identify actions that fail to reflect such values. Promotion decisions should also be based on the ethical values.

When employees are promoted only on the basis of their financial performance when they have not lived up to values only enforces the perception for other employees that the firm does not consider ethical values to be important. This can have a potentially severe impact on the firm's ethical corporate culture. Disciplinary or even dismissal decisions should also be based on whether individuals live up to values. Most important is that, to the greatest extent possible, the firm aligns its reward system - including compensation - with its ethical values.

Practices

If the firm has a set of core ethical values, it needs to be perceived to live up to them; that is, it must 'walk the talk.' Without this general perception, ethical values quickly become meaningless. To prevent this from occurring, there are a variety of practices

that should explicitly incorporate the firm's values. All decision making and behavior at every level and function should be based on the firm's ethical values, whenever possible. This includes not only at the executive, manager and employee levels, but also at the board of directors level. Surveys of employees and customers should attempt to include feedback on performance of the firm and its agents with respect to ethical values. All meetings, additional training efforts, and speeches - especially by senior managers - should make explicit reference to core ethical values. The aforementioned actions reinforce core ethical values, helping to sustain an ethical corporate culture.

Another method entails building ethical values into stories about the actions/decisions of employees, managers, or senior executives, which gives greater meaning to the organization's culture. This storytelling should include positive tales in which an employee, manager, or even the chief executive officer (CEO) acted consistently with the firm's core ethical values, despite financial pressure to do otherwise. However, it should also include negative stories whereby the firm failed to live up to its values, as well as discussions about why the mistakes were made and how to avoid such mistakes in the future.

Second Pillar: Formal Ethics Program

Most commentators agree that a formal, comprehensive ethics program is necessary to help establish and ensure an ethical corporate culture, particularly for larger organizations. In fact, changing regulations have virtually made it a requirement for large firms and public firms to ensure they have such programs in place. For example, the U.S. Federal Sentencing Guidelines for Organizations (FSGOs), which were enacted by the U.S. Sentencing Commission [1], are referred to when judges sentence organizations for violating U.S. federal law. The FSGOs permit firms to have their fines reduced if they are able to establish that they possessed an effective compliance and ethics program prior to the offense. Revised in 2004 and again in 2010, the FSGOs now suggest that an ethical organizational culture is necessary before a firm can be considered to have an effective compliance

and ethics program designed to prevent illegal and unethical behavior.

The FSGOs (Section 8B2.1) state: "To have an effective compliance and ethics program, an organization shall promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law" [emphasis added]. The FSGOs go on to identify the minimum requirements for a firm to be considered as possessing an effective program, including a code of ethics, ethics training, an individual responsible for the ethics program, and a reporting system for improper behavior.

In a similar fashion, the U.S. Sarbanes-Oxley Act (SOX) requires firms to ensure the presence of certain ethics program elements. Not only are public firms essentially required to possess a code of conduct or ethics, but SOX also suggests certain minimum content for the code while requiring that firms have appropriate whistleblowing channels. Numerous commentators now also provide more specific recommendations regarding each element of an effective ethics program. For example, codes of ethics should be easy to understand and non-legalistic, include relevant examples, avoid a negative tone, and include expected behaviors and sanctions. The code development process should involve employees, apply to everyone in the organization, and include a sign-off process whereby employees indicate they have read, understand, and will comply with the code. Ethics training with relevant examples should be conducted by managers whenever possible. The code should be reinforced regularly at meetings and through emails, newsletters, and high-level speeches.

Often referred to as an ethics or compliance officer, an administrator who has direct access to the board of directors and who cannot be fired by the CEO should be appointed to oversee the ethics program. To the greatest extent possible, a reporting mechanism should also be established to provide for anonymity and confidentiality with no fear of reprisals; any code enforcement must be fair and consistent. Finally, regular monitoring and auditing of the ethics program's effectiveness should take place, as well as periodic revisions.

All these measures are part of developing a comprehensive and effective ethics program. Ultimately, the program should be based on the previously discussed core ethical values. However, a firm that possesses core ethical values infused throughout its policies, processes, and practices - even when supported by a comprehensive ethics program - is not sufficient. The presence of ethical leadership is also necessary, as will now be discussed.

Third Pillar: Ethical Leadership

Beyond infusing ethical values throughout the organization and developing a comprehensive ethics program, to achieve an ethical corporate culture, there must also be an ethical tone at the top. In fact, many suggest that an ethical corporate culture is contingent upon ethical leadership: "The moral tone of an organization is set best by top management...workers generally get their ethical cues by observing what their bosses do" [13]. According to Brown, Trevino, and Harrison [14], "Leaders should be the key source of ethical guidance for employees." They define ethical leadership as "The demonstration of normatively appropriate conduct through personal actions and interpersonal relationships, and the promotion of such conduct to followers through two-way communication, reinforcement, and ethical decision-making".

Others have even suggested that a relationship exists between ethical leaders and the presence of values within an organization: "Ethics is central to leadership because of the...impact leaders have on establishing the organization's values" [15]. Of course, ethical leadership must be demonstrated not just by the CEO and other senior executives in the C-suite, but at every level, including first-line supervisors and retail store managers. The relationship between ethical leadership and ethical behavior has also been observed.

According to Hitt [16], "results of research studies demonstrate that the ethical conduct of individuals in organizations is influenced greatly by their leaders." Perceptions among employees that their managers possess a set of core ethical values and act upon them has been shown to significantly impact the firm's ethical corporate culture. Based on a

survey of more than 10,000 U.S. employees, a study by Trevino, Weaver, Gibson, and Toffler [17] supports this point: When employees perceived that supervisors and executives regularly pay attention to ethics, take ethics seriously, and care about ethics and values as much as the bottom line, all of the outcomes [i.e., employees less likely to engage in unethical/illegal behavior, have greater awareness of ethical/legal issues, more likely to look for advice within the firm, willing to deliver bad news to management, willing to report ethical violations, and more committed to the organization] were significantly more positive. Despite the recognized importance of ethical leadership within business, there appears to be a perception that such leadership is lacking. Foreexample, a 2010 Gallup survey of more than 1,000 U.S. adults found that only 15% perceived business executives as having 'very high' or 'high' honesty and ethical standards, even lower than auto mechanics at 28% and TV reporters at 23% [18]. In a 2009 survey of 1,024 of its readers from around the world, Harvard Business Review found that 76% of respondents had less trust in U.S. senior management than they had the previous year, and 51% had less trust in senior management at non-U.S. companies [19]. This suggests that there is significant room for improvement in society's perception of business leaders' ethical values.

Why do most people, including employees and government regulators, remain so skeptical of corporate executives' ethical leadership capabilities? One reason is the inherent conflict between executives' desire to act in a manner that fulfills their fiduciary obligations to shareholders (i.e., maximize the bottom line) versus engaging in what the public considers to be ethical behavior (i.e., putting people before profits). For the general public, which does not possess a fiduciary obligation to stockholders, this perceived conflict of interest and corresponding perceptions of excessive corporate and executive greed is arguably the underlying basis for the anti-Wall Street movement. For governments, such perceptions appear to drive continuous calls for enhanced corporate governance regulations to restrain errant conduct. Thus, how exactly can managers and executives

exemplify ethical leadership and reverse current negative perceptions? Creating perceptions of ethical leadership is no easy task. Because most employees will not have direct contact with their senior managers, the firm's leaders must attempt to develop a reputation for ethical leadership. Various studies have examined how an ethical reputation is developed. Trevino, Brown, and Pincus-Hartman [17] suggest there are two dimensions to ethical leadership: a 'moral person' dimension and a 'moral manager' dimension.

The moral person dimension requires the manager to act with integrity, honesty, and trustworthiness. It is based on the manager treating people with respect and dignity, and living a moral life at the personal level. The moral manager dimension is affected not only by visibly role-modeling ethical conduct but also by applying a reward system to hold everyone accountable, and by regularly and openly communicating with all employees about the importance of ethical values. If one is perceived as being a strong moral manager but a weak moral person, he/ she would be seen as a hypocrite; that is, he/she talks about the importance of ethics but does not act accordingly. To be an ethical leader, a manager must be perceived as both a strong moral manager and a strong moral person. Probably the most significant means of demonstrating ethical leadership is to ensure that all decision making is in accordance with the aforementioned ethical values. This becomes increasingly apparent when executives are seen to make such decisions even at great financial cost to the firm. Ethical values must be seen to take priority over other interests, or they quickly become irrelevant.

In one famous example, as the founder of his accounting firm, the then-28-year-old Arthur Andersen refused to yield to the questionable demands of an important railway client during an audit. He lost the client as a result, but when the client later went bankrupt, Arthur Andersen developed a reputation as someone who could be trusted to act with integrity. This decision set an ethical tone for the firm for many years, leading to Arthur Andersen later acting as a watchdog over the entire accounting industry. Unfortunately, such

ethical behavior did not continue in the long term at Arthur Andersen, and its culture - especially in relation to its client, Enron - began to focus more on generating revenue than on the ethical values originally underlying its auditing business.

In another high-profile case, former Johnson & Johnson CEO James Burke relied on his firm's credo to withstand the 1982 Tylenol crisis and derive a long-term competitive advantage from the event. Under Burke's leadership, the company placed customer safety ahead of financial considerations: it recalled Tylenol nationwide, despite the massive cost. Similarly, former Alcoa CEO, Paul O'Neil, developed a reputation for caring about the safety of his employees. He did this by visiting plants and indicating to personnel that there would be no budget limits for safety matters; they should spend as much as necessary to fix all safety hazards, regardless of the cost.

O'Neil distributed his home phone number such that safety problems could be reported, and he flew to speak in person with employees who had been injured on the job. As another example, following a series of scandals at the Canadian bank CIBC related to its dealings with Enron and a \$2.4 billion settlement with investors, the new CEO, Gerald McCaughey, decided to voluntarily accept a compensation package that delayed the vesting of his share options extensively and also included a provision that his compensation could be taken away retroactively if a scandal was later discovered to have occurred during his term as CEO of the bank. Such actions could be seen to demonstrate a commitment to ethical values, including integrity, caring, and responsibility, leading to a perception of the CEO as an ethical leader.

Unfortunately, however, a multitude of companies have failed to establish such an ethical tone at the top, leading to significant scandals that sometimes caused their downfall. For example, U.S. firms and their former CEOs, such as WorldCom (Bernie Ebbers), Tyco International (Dennis Kozlowski), and Adelphia (John Rigas); Canadian firms, such as Hollinger (Conrad Black) and Livent (Garth Drabinsky); and the Italian firm Parmalat (Calisto Tanzi)

appear to have lacked an appropriate tone at the top.

These examples represent firms with unethical leadership, leading to behavior that cost them “billions of dollars a year due to increased absenteeism, health care costs, lost productivity, and expended costs associated with defending actionable claims” [20].

In other cases, highly successful CEOs, such as Harry Stonecipher of Boeing and Mark Hurd of HP, were forced to resign following the discovery of inappropriate relationships. Even Enron - despite possessing a comprehensive compliance and ethics program - collapsed at least in part due to an unsuitable tone at the top led by former CEO Jeffrey Skilling, who emphasized bottom-line results over ethical values. Kenneth Lay, also former CEO and chairman of Enron, demonstrated a lack of ethical leadership when he requested that Enron’s managers use his sister’s travel agency for all of their overseas flights. Similarly, the U.S. government bailout of American International Group (AIG), the collapse of Lehman Brothers, and the sale of Merrill Lynch appear to demonstrate how the self-interested pursuits of these firms’ senior leaders led to severe financial repercussions for their investors, clients, employees, and other stakeholders. All of these examples seem to support the claim that “Leadership which lacks ethical conduct can be dangerous, destructive, and even toxic” [21]. To summarize, an ethical leader is trustworthy, honest, transparent, responsible, caring, respectful, and fair; acts with integrity; and puts the interests of the firm and other stakeholders before his/her own personal interests. All of this must be demonstrated through the leader’s actions, not just through words. In fact, only greater cynicism among employees will occur if the leader talks about the importance of ethical behavior but does not act accordingly. Regardless of the financial implications, senior executives’ failure to act ethically must lead to disciplinary action by their firm’s board of directors, in order to ensure a sense of accountability. Without ethical leadership across the organization, including at the board of directors level, there is little chance of establishing and sustaining an ethical corporate culture.

Discussion and Conclusion

Figure 1 summarizes the interaction of all three elements necessary to develop and sustain an ethical corporate culture within a firm. Once an ethical corporate culture is developed and hopefully sustained, the assumption is that the extent of crime, corruption, and unethical activity within organizations or on their behalf will be minimized. Of course, developing an ethical corporate culture is only the first step, as multiple challenges must continually be overcome. For example, developing and sustaining an ethical corporate culture becomes exceptionally difficult for large multinational organizations with tens if not hundreds of thousands of employees around the world, each with his/her own distinct ethical perspective and culture.

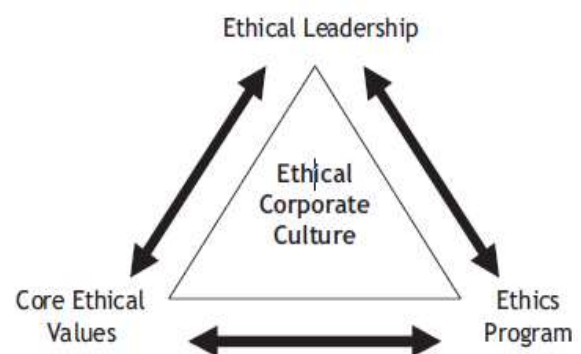


Figure 1: Key elements of an ethical corporate

As a multi-pronged approach, all of these stakeholders can collectively place additional pressure or create incentives to encourage firms and their agents to engage in legal and ethical behavior. With respect to firms’ own efforts, there are three fundamental elements that form the basis of an ethical corporate culture: (1) the existence of a set of core ethical values, (2) the establishment of a formal ethics program, and (3) the continuous presence of ethical leadership. As a summary, Table 2 highlights the key recommendations and provides better-known corporate examples of the good and bad for each of the three pillars of an ethical corporate culture. With significant corporate scandals taking place in 2010 - such as Toyota’s recall troubles, leading to approximately \$50 million in fines and billions of dollars in related expenses; Goldman Sachs betting against a sub-prime mortgage product while simultaneously recommending the

product to its own clients, leading to a \$550 million settlement; and BP's massive oil spill in the Gulf of Mexico, spurring

establishment of a \$20 billion compensation fund - one might question whether these firms had all three elements clearly present.

Table 2: Three pillars of an ethical corporate culture: Recommendations and examples

	Recommendations	Examples
1)(a) Core ethical values :policy	Establish a set of core ethical values for the firm, including trustworthiness, responsibility, caring, citizenship, fairness, and respect. Emphasize that when in conflict, the ethical values must take priority over the bottom line. The ethical values should be posted prominently in the firm's code of ethics and on the home page of the firm's website.	Good: Johnson & Johnson's credo establishes stakeholder priorities by stating that its first responsibility is to the users of its products and services while its final responsibility is to its stockholders. Bad: Toyota's actions leading to the brake pedal recall appeared to equate the value of 'safety' with 'quality' rather than making safety a priority in and of itself.
1) (b) Core ethical values: Process	An ethical values filter should be applied to decision making, including hiring, performance appraisals, and firing. Whether one acts in accordance with the ethical values should be directly tied to the firm's compensation/reward system.	Good: The firm Veritas (Latin for truth) fired its chief financial officer when it was discovered that he had lied on his resume years before about having a master of business administration. Bad: Enron's performance appraisal system (i.e., the 'rank and yank' process of dismissing the bottom 10% of performers) appears to have contributed to pressures to cut ethical corners.
(1) (c) Core ethical values: Practice	All firm-level and managerial-level decision making should be based on and explicitly refer to the core ethical values whenever possible.	Good: Bank Boston's application of the ethical value of respect during layoffs in the 1990s led to the provision of job retraining, educational grants, and support of non-profit employment for employees who were laid off. Bad: Enron's complete disregard for its explicit values as indicated in its code of ethics, including respect and integrity (i.e., honesty)
(2)(a) Formal ethics program: Code	Ensure employee involvement in code creation or revision to help achieve buy-in and ensure realism. Code should apply to all firm's agents, including contractors and suppliers.	Good: Wal-Mart's 'Statement of Ethics' applies to all relevant stakeholders, including the firm's suppliers, consultants, law firms, public relations firms, contractors, and other service providers. Bad: WorldCom lacked a code of ethics based on CEO Bernie Ebbers' view that having such a code was a "colossal waste of time."
(2)(b) Formal ethics program: Implementation	Annual sign-off of the code should take place. Relevant examples should be used during training. Manager should conduct training whenever possible.	Good: Johnson & Johnson periodically surveys its employees to evaluate how well the company lives up to its credo responsibilities. The firm ensures that the credo remains at the heart of the corporate culture by training its managers in the credo-based Johnson & Johnson Standards of Leadership. Bad: Enron's training video 'Vision and Values' includes CEO Jeffrey Skilling's statement: "Out there. . . there's a desire to cut corners, but we can't have that at Enron."
(2)(c) Formal ethics program: Administration	A well-communicated whistleblowing channel should be established with protections provided against retaliation. Refer to the whistleblowing channel as a 'helpline' rather than a 'hotline.' Annual audit of the ethics program's effectiveness should take place with modifications made if necessary.	Good: Following its bribery scandal, Siemens created an ethics and risk compliance department with 600 employees, developed a training program, and changed the reporting system at the highest levels to try to prevent future misconduct. Bad: BP's alleged failure to protect its employees who raised safety complaints, in part leading to the Gulf oil spill.
(3) Ethical leadership	All actions and decisions at all levels throughout the organization should exemplify ethical leadership up to and including the board of directors. Managers should ensure that their personal behavior does not conflict with their ethical reputation at work.	Good: Johnson & Johnson's CEO James Burke's decision to recall Tylenol nationwide based on the company's redo and despite the financial cost. Bad: HP CEO Mark Hurd's concealed relationship with a marketing consultant and his submission of inaccurate expense reports.

Without all three of these elements firmly in place, each of these firms arguably developed corporate cultures that emphasized financial considerations over the health, safety, or general wellbeing of other stakeholders. For example, some suggest that Toyota has a secretive

corporate culture in Japan that disagrees with disclosing safety defects [22], and Goldman Sachs' corporate culture focus on revenue generation, egos, and bonuses is viewed as contributing to its clients being misled [23]. Similarly, a U.S. government commission referred to BP as possessing a

culture of complacency, with profits taking priority over safety, which partially led to the Gulf oil spill [24]. Future research might examine the extent to which firms like these that suffer ethical scandals are deficient in terms of infusing ethical values throughout the organization, possessing a weak ethics program, and/or lacking ethical leadership. Research might also examine whether such firms succeed in developing and sustaining ethical corporate cultures following such incidents based on the presence of the three core elements or if any changes in ethical culture tend to be merely short term in nature.

While all three elements are distinct, they also reinforce and support each other. For example, ethical values become the basis for ethics programs, which can in turn enhance ethical leadership. As discussed, ethical leadership is critical for the successful infusion of ethical values throughout the organization and the potential effectiveness of ethics programs. When all three elements

of an ethical corporate culture are in place, employees are not only sensitized to recognize the ethical dilemmas they or their firms face, but will also hopefully have the motivation, ability, and confidence to respond in an ethically appropriate manner with such ethical behavior being supported and rewarded by all managerial levels of the organization. Such ethical sensitivity will hopefully not only take place for macro-level ethical issues, such as whether to open up operations in a country run by a repressive regime, but also for micro-level issues, such as whether to hire a friend who is highly qualified for a job position. Nevertheless, due to human nature, crime, corruption, and other factors, illegal or unethical activity will never be completely eliminated for a certain percentage of the workforce regardless of whatever efforts are undertaken. However, business firms have an ethical obligation to make reasonable attempts to minimize the presence of crime and unethical activity for the good of all society.

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