Ethical Failures Are a Growing Concern

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Rising costs

It's becoming personal

Domino effects

Regulators expect more

Framing Ethical Risk – A Few Examples

Wells Fargo

Cross-selling credo

Pressure to perform from leaders

Incentives tied to results

Retaliation

Strong local autonomy

BP

Focus on profit and pressure to grow

Bottom-line mentality

Heavy risk-taking

Looming deadlines

Kobe Aluminum

Focus on profit + efficiency + quality

Pressure to perform from leaders

Incentives tied to results

Highly conforming culture

Strong local autonomy

Volkswagen

Focus on growth and perfection

A demanding CEO and a special type of pressure

Speaking out was heavily sanctioned
The Two Culture Dimensions That Create the Most Risk

Culture is the organizing principle of what a company values

- Delegation of Ethical Dilemmas
- Ethical Capacity

Understanding the Link Between Culture, Ethics, and Risk

1. The more the pressure points, the harder it is to make good decisions. In a VUCA world:
   - Policies fall short
   - Values are easily overridden
   - A gap between stated values and what the organization actually values
     - Creates ambiguity and uncertainty
     - Adds complexity to what people in have to address on a daily basis

2. People overestimate the sturdiness of their ethics:
   - Unethical behavior is much more likely when people experience conflict of interest and find ways to rationalize their conduct
   - Cognitive and emotional depletion affects our ability to do the right thing
   - It’s easier to fend off explicit requests than pressure to perform
SAI's Global Strategic Culture Framework: Part 1

**Principles of Conduct**
- Conflicting principles turn into competing priorities
- Competing priorities create pressure
- Pressure leads to disengagement
   - Bonus point:
     - Values can affect a false sense of morality
     - Priorities that delegating the role of ethics reinforces the belief that others are less ethical than us

**Delegation of Ethical Dilemmas**

**Leadership & Power**
- Manager conduct is a key driver of an ethical culture
- Power asymmetries make managers' requests impactful
- Leaders' moral maturity impacts their employees'
- Leaders who ignore ethics accelerate unethical practices and can have consequences of moral degeneration

**Rewards & Sanctions**
- Incentives make unethical conduct more likely if
  - They aren't connected to specific goals
  - Are associated with specific goals
  - Managers do not show any vulnerability in relation to competing priorities

**Symptoms of Delegation of Ethical Dilemmas**
- Lack of principles or unclear principles - people can figure it out
- No ethical decision is made
- Values are in conflict
- Ethics is unimportant
- It's ok to talk about values, but let's get back on track and focus on business
- We can't keep talking about revenue
- Water under the bridge
- Not talking about the issue
- Not discussing results and not taking responsibility
- Telling people to just get it done
- Taking power to patronize expertise and competence
- Managers don't show any vulnerability in relation to competing priorities

- There are clear rewards for achieving results but not clear penalties for substandard performance
- There is an annual ethics award, but everybody evaluates career prospects based on performance only
- Value for not meeting performance goals: record penalties for acting unethically
- Abuses of power are treated with a slap on the wrist
- People cannot stop talking about revenue
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Delegation of Ethical Dilemmas in the Banking Sector

- 67% Agree
- 33% Fail to Agree
- Misconduct has cost the banking sector more than $200 billion over the past 10 years
- The larger the gap, the more likely employees are to report that their firm is prioritizing profit over customer outcomes
- The smaller the gap, the more likely employees are to indicate that leaders walk the talk

Ethical Ownership
- Who owns the organization's ethics?

Ethical Capacity
- Culture facets that shape how the organization responds to ethical issues

Evidence That Ethical Capacity Works Like a Muscle

Ethical Ownership
- Diffusing responsibility and/or minimizing the consequences of our actions reduces agency and increases moral disengagement
- If we feel responsible, we pay attention to our behavior; if others set standards for us, we wait on them to make decisions for us

Ethical Reasoning
- Selective recollection: retaining the positive while forgetting the negative
- Loyalty to group creates justification for unethical behavior
- Unfairness increases cheating
- Competition, especially in the presence of specific goals, leads to unethical behavior
- Creativity generates cognitive ease and a false sense of control

Ethical Voice
- Confidence in self and available means increase employee engagement
- Fear of failure suppresses voice
- Fear of retaliation belongs to an unethical conduct

SAI's Global Strategic Culture Framework: Part 2

- Ethical Ownership
- Ethical Reasoning
- Ethical Voice

Ownership
- What conditions support ethical reasoning?
- Can people correct ethical issues?
Ethical Capacity in the Banking Sector

- People do not avoid responsibility
- Firms with less accountability are characterized by silos
- These firms do not solicit employee feedback before implementing change
- A fear and blame culture is quite widespread in these organizations
- The cost of misconduct in the banking sector is likely to approach $400 billion by 2020

Symptoms of Low Ethical Capacity

- Ethics and compliance are treated as a requirement
- When an ethical issue arises, you hear “This is not our problem, let’s call the compliance team”
- There is a tendency to assign blame (e.g., departmental blame)
- Employees believe it’s more important to fit in than to do the right thing
- When an ethical issue arises, you hear “This is not our problem, let’s call the compliance team”
- There is no time to address pressure points, grey areas, and implications for behavior
- Conversations about voice, diversity, and inclusion, and ethics are shallow
- People believe that it’s better to keep low and quiet
- If an ethical issue arises, you hear “This is not our problem, let’s call the compliance team”
- Employees have no idea how the information they share is used
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Predicting Risk – Wells Fargo

<table>
<thead>
<tr>
<th>Culture Determinants</th>
<th>Wells Fargo’s Profile</th>
<th>Level of Risk</th>
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</thead>
<tbody>
<tr>
<td>Principles of Conduct</td>
<td>Change is also driven by the company, Wells Fargo positioned its commitment to the customer and fostering trust. On the other hand, it pushed employees to meet goals, as a result, sales were priorities.</td>
<td>〇</td>
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<tr>
<td>Leadership &amp; Power</td>
<td>Leadership and power were decentralized, local leaders used metric-driven sales strategies, and incentives. This led to pressure on employees to meet targets and sold products.</td>
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<tr>
<td>Incentives &amp; Sanctions</td>
<td>Incentives were tied to sales performance, target incentive was tied to the overall performance of the organization. This led to pressure on employees to meet targets and sold products.</td>
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<td>Ethical Voice</td>
<td>Wells Fargo fostered a culture in which threats, intimidation, and retaliation played a significant role. Eventually, 5% of the workforce denounced the sales practices that occurred across the organization.</td>
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</tbody>
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Ethical Ownership

- According to Wells Fargo, the businesses owned ethics. Yet, leadership framed the scandal as a “compliance and operations” problem.

Ethical Reasoning

- The compliance and ethics program trained employees to spot conflicts of interest and provided them with a Code of Conduct. Though valuable, these resources were insufficient to cope with the sales pressure employees faced daily.

Ethical Voice

- Wells Fargo fostered a culture in which threats, intimidation, and retaliation played a significant role. Eventually, 5% of the workforce denounced the sales practices that occurred across the organization.
Where Is Your Organization Today?

Two Guiding Questions

- Is your organization delegating dilemmas?
- What’s your organization’s ethical capacity?

Mature: Low delegation of dilemmas, high ethical capacity.

Righteous: High delegation of dilemmas, moderately high ethical capacity.

Ambivalent: High delegation of dilemmas, low ethical capacity.

Immature: Low delegation of dilemmas, low ethical capacity.

Risk is low; growth is ethical.

Risk is moderate; focus on principles and strategies; compensation in-lieu of ethical capacity.

Risk is moderately high due to intense pressure despite ethical capacity.

Risk is very high; growth is not sustainable.

Assessment Process: Key Considerations

**PRINCIPLES OF CONDUCT**

- What are the organization’s stated values? What do they mean?
- What does the organization value in the face of difficult decisions?
- What criteria are given priority within specific contexts (e.g., hiring, promoting, etc.)?
- How frequent are certain dilemmas?
- What conditions are likely to override ethical considerations?

**LEADERSHIP AND POWER**

- Are leaders walking the walk?
- How do leaders exercise power?
- What criteria are used to hire and promote leaders?
- How do leaders behave under pressure?

**REWARDS AND SANCTIONS**

- What are the organization’s formal rewards/sanctions?
- What is implicitly recognized, rewarded and sanctioned?
- What behavior gets reinforced in case of a trade-off between ethics and business?

**ETHICAL OWNERSHIP**

- What’s the responsibility of business?
- How does compliance work with business leaders?
- How are ethics framed in the organization?
- What goals do stakeholders hold in relation to ethics?
- How is stakeholder accountability monitored?

**ETHICAL REASONING**

- What resources do currently support ethical reasoning?
- What factors constrain reasoning at work?
- What level of dilemma are people able to detect?
- Is there an open/honest dialogue about pressure points?

**ETHICAL VOICE**

- What channels are available? How effective are they?
- Where/how can people practice their voice?
- What’s the value/cost of voice and silence?
- How does the organization follow up on voiced dilemmas?
- Do people feel in control of voice practices?
A Pathway to Proactive Risk Mitigation

Linking Culture to Ethics and Risk: Using the Strategic Culture Framework

- Assess key systems using the framework to determine which resources and how they can help reduce dilemmas and increase ethical capacity.
- Leverage the organization's ethical capacity against the level of risk associated with dilemmas.
- Hold key stakeholders accountable by focusing executive conversations, business planning, and board activities on the delegation of ethical dilemmas occurring in the organization at any given time.
- Re-design systems and key resources to fully incorporate the framework's principles.

Measure

1. The impact of your E&C program
2. Your organization's culture
3. Ethical risk