Business Ethics

The Path to Certainty

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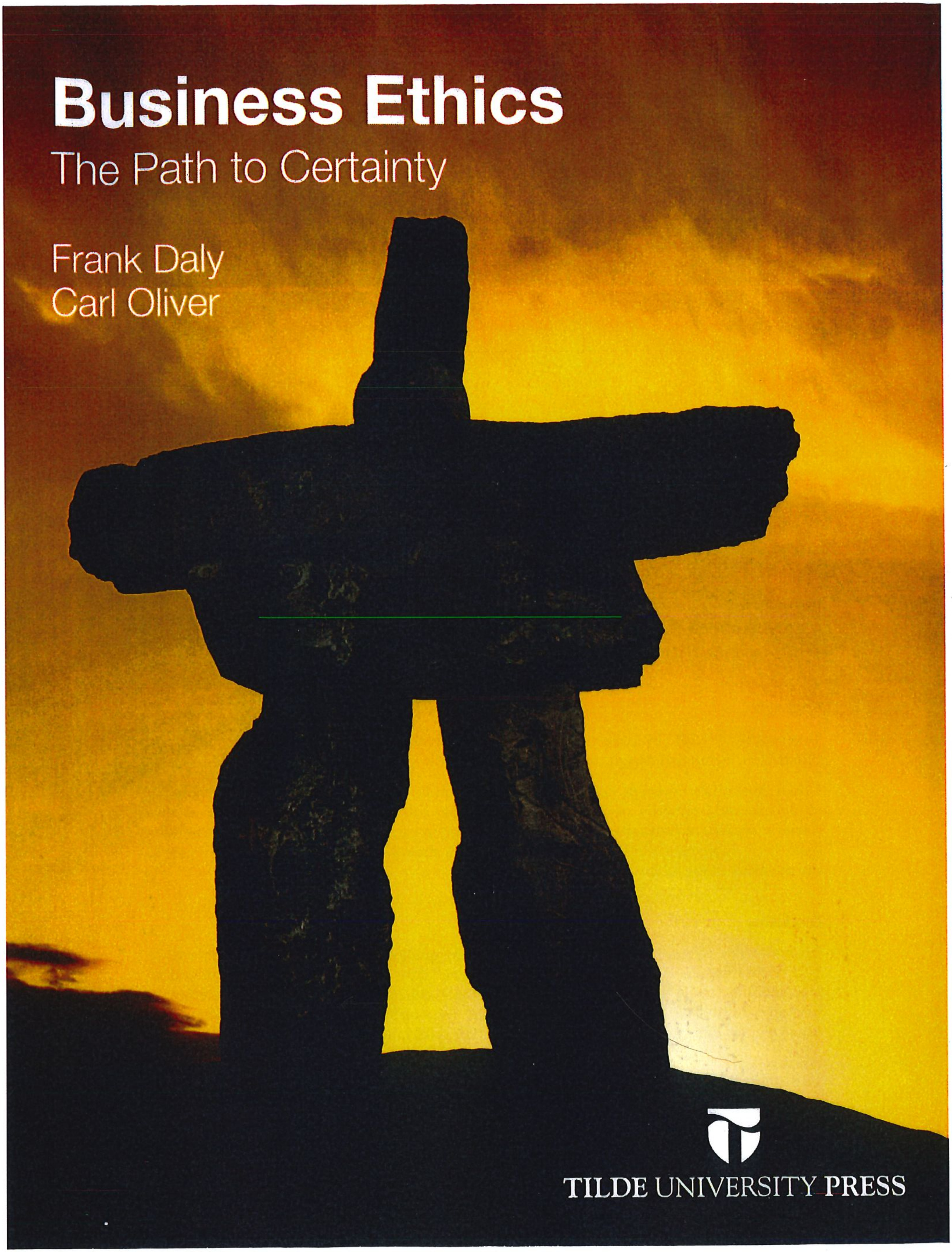

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Chapter 2

The True Driver

FALLACY 1:
TO STOP ETHICS FAILURES WE NEED ONLY TO HAVE RULES, TEACH PEOPLE THE RULES, AND PUNISH ANYONE WHO VIOLATES THOSE RULES

Alpha Corporation [a pseudonym] faced a crisis, of violations of US export laws. This was no minor problem. The company's survival was at stake. As part of its legal defense, Alpha deliberately created a corporate ethics program, hired a new, full-time corporate ethics director and expected the director to focus on compliance with laws and regulations.

The devil must cheer when a company, like Alpha, innocently, unwittingly and mistakenly focuses its business ethics narrowly on compliance with laws, regulations and rules, and then appoints an ethics 'czar' to take charge, perhaps aided by a few people in a silo organization. That sets the stage for business ethics to fail because those conditions free most leaders throughout the company from feeling responsible for ethics. They frame ethics as someone else's job. They allow and perhaps even encourage employees to see business ethics as just an administrative square-filler. They ignore two fundamental truths: (a) that ethics is in everyone's job description and (b) that leaders must feel personal and professional responsibility for the ethics of their company.

'Framing' contributes to business ethics uncertainty. A frame offers perspective on an issue. It can help us consider, overlook, or organize thoughts about aspects of an issue. With respect to business ethics, people often use too narrow a frame. They often expect to focus just on compliance with the law. That frame creates Fallacy 1, the idea that ethics requires only making rules, teaching rules, and punishing anyone who violates those rules. We need to adopt a broader, more long-term perspective. It is necessary to have rules, teach people the rules, and have consequences for those who violate the rules. However, in the words of notable business ethics advisor Jeff Kaplan, that is 'necessary but not sufficient'.

Luckily for Alpha, the new ethics director realized the company was using too narrow a frame. The director sent an email to colleagues in the business ethics community: 'I have defined my role as covering governance, compliance, and ethics. As a lawyer, I am much more comfortable in the first two realms since I can generally identify the source of the rules. In the realm of ethics, I could use some definition and navigational advice'.

Let's be clear early on, so no one misunderstands: nothing in this book impugns lawyers or plays to the lawyer jokes crowd. For reasons we will explain later, we see placement of ethics within a company's legal department as a problem and we recommend against it. Nevertheless, whoever a company appoints to lead ethics must establish and nurture a close, open relationship with the company's lawyers. They are vital members of a corporate ethics team.

Anne Takher stands as an example of a lawyer who has undertaken to foster close relations between lawyers and ethics officers. Her focus is 'preventive law'. She has become an anti-bribery expert and will tell you 'preventive law' plays such an important role in corporate compliance that she has built her career around it. Her objective aligns exactly with the ethics officer's goal: keep companies and their employees out of trouble in the first place. We focus this book on ways to do that while appealing to what Abraham Lincoln called 'the better angels of our nature'.[1]

Thus, it is not only lawyers who play important roles. Leaders in the professional business ethics community encourage a team effort, where:

- the law department helps to identify compliance rules and to design training so that employees know the rules and how to meet them;
- the accounting and finance department helps to design and test financial controls;
- the internal audit department helps to evaluate and test procedures and policies; and
- the training department helps to educate employees so they are able to meet compliance requirements and understand how all these efforts relate to the company's stated values.

We recommend a team effort encompassing the entire company and extending to other companies, including competitors, so all are ethical equals, playing on a level field and performing at the highest possible level of ethics. We're thinking of membership in business ethics groups like the Defense Industry Initiative on Business Ethics and Conduct (DII) or the Ethics and Compliance Officer Association (ECOA). Such membership delivers important advantages in terms of learning, networking and getting your company's name out as one that is serious about ethics. While the news media may express some interest in a company's ethics effort as an initial novelty or when the company gets in trouble, the best way to communicate to others about your company's ethics is through multi-company ethics group meetings attended by peers, vendors and regulators.

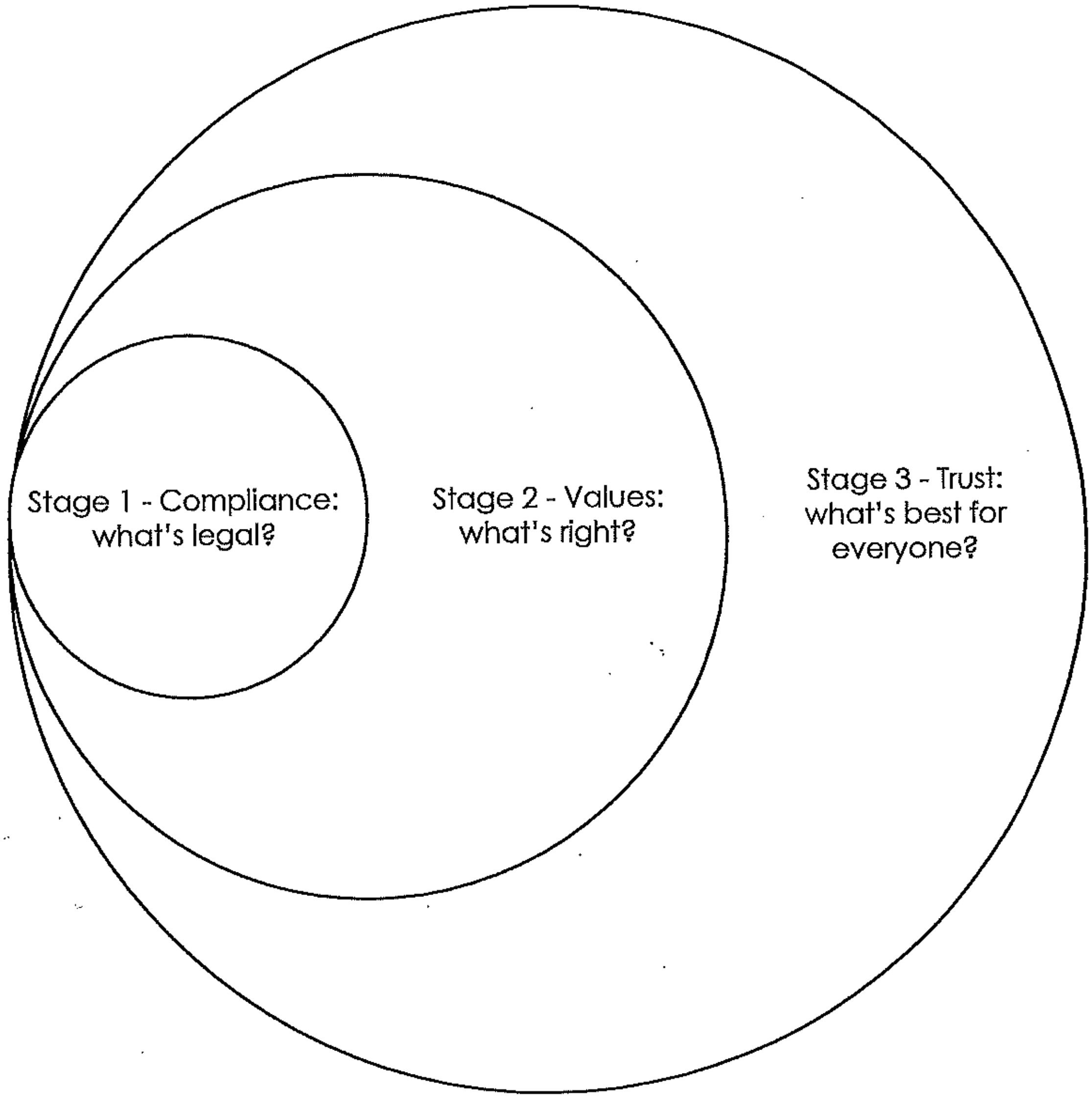
More about that later. First, let's help ethics officers – and business owners, and managers and supervisors, and business leaders in general – by answering the question about definition and navigational advice in the realm of business ethics.

The ethics dynamic

The ethics dynamic model provides a broad frame that supplies both definition and navigational aids. A Venn diagram (Figure 2.1) shows the three stages of the ethics dynamic model, dramatizes why laws, regulations, and rules deserve to be recognized as a necessary but small part of business ethics, and clarifies why the frame of reference should expand to include values and trust as the dominant traits and drivers of effective business ethics.

Stage 1, compliance, is all of laws, rules, and regulations. Stage 2, values, encompasses all of Stage 1 and adds decision guidelines based on values. Stage 3, trust, encompasses all of Stages 1 and 2 and adds strategic decision guidelines based on building trust.

Figure 2.1 Venn diagram of the ethics dynamic



Stage 1 is compliance

Many companies start here because they are in crisis mode, responding to allegations that they have violated the law. Sometimes they start here because they want to respond to new laws and regulations, like the US Sentencing Guidelines for Organizations or the *Sarbanes-Oxley Act* of 2002. They want to teach employees the law so that they can avoid new allegations. The primary question at Stage 1, the *compliance* question, is: what is legal or illegal? What are the rules? Teach employees the rules so they will not commit new violations.

Nothing is inherently wrong with that! Employees who know and abide by laws and rules protect the company and themselves from bad consequences like investigations, fines, trials, and jail. Moreover, following the law does send a supportive message honoring the larger community, a message that benefits society in general. People who know and follow the rules respect community social values that contribute to order and civility in both the workplace and broader society. In fact, a narrow focus on the law robs it of these larger communitarian values.

This is a strength of Stage 1. It is important that rules and laws exist as clear guidelines for those who might need them. Company climate and culture always must send the message that compliance, respect for the law, and responsibility and accountability to society are valued in the organization.

Yet Stage 1 alone does not work. Stage 1 characteristically focuses on rules, more rules, and still more rules. Infinitely more rules? That is not practical for long. Scholars find themselves formally stating an obvious truth: 'there is simply no way to create enough rules to cover even the most ethically important occurrences, even if they could be identified before they occurred'.[2] A code of ethics overloaded with rules becomes ineffective; even if some people are willing to wade through reading it, few are likely to remember much of what they've read. To illustrate, we ask our students how many have drivers licenses — it's everyone — and then how many have read the state motor vehicle code (not the driver handbook summary of laws, which has now grown to 108 pages, but the full vehicle code that is now nearly 1,000 pages long). Everyone drives, but none of our students has ever tried to read all of the rules.

Many companies, however, don't advance beyond Stage 1 because of 'tone-at-the-top', the attitude and perspective of the company's most senior leaders. Our analysis suggests a number of reasons why:

- Small company or large, the leaders look outside the company for vendors who can supply ethics expertise. Especially since Congress enacted the *Sarbanes-Oxley Act* of 2002, law and accounting organizations that focus on their compliance expertise aggressively market such services.

- For perspective, the leaders seek guidance from academics, some of whom teach the intellectual issues of business ethics but misperceive the business ethics practitioners' role as limited to compliance. Some academics appear to think ethics and profit are not compatible and that the evaluation and guidance business ethics practitioners bring to companies are not really ethics. That's a strange position because it suggests that work — an activity millions engage in for at least one-third of their waking hours — is not worthy of any ethical evaluation except condemnation when errors become apparent.

- Culturally, the leaders allow themselves to be influenced by news media reports that highlight initiatives by government ethics committees almost universally focused on compliance with rules and laws and on punishing offenders.

- Organizationally, the leaders choose to assign ethics responsibility to their general counsel's office or law department because it is chartered to protect the company from harm — a compliance with laws approach.

We observe, unfortunately, that many if not most programs are almost exclusively compliance oriented and report to the organization's law department. We do not deny the necessity of compliance. Jeff Kaplan, who is an attorney in addition to being a bright star in the field of business ethics, identifies the greatest fallacy in designing business ethics programs as the belief that because promoting compliance with laws and regulations is necessary it is also sufficient, and that a company therefore need not also address the need for ethical analysis and conduct.[3] People must know the rules – key rules even when it is impossible to remember all the rules – but they also must be motivated, supported, and rewarded for making good decisions when there might not be a rule or the rules aren't clear. That's when the organization's values, customs, and culture guide them.

Observers usually see companies move progressively from Stage 1 to Stage 2 to Stage 3 as they gain experience, as their ethics program matures, as it evolves with time.[4] However, companies and subcultures within companies can operate at any of the three stages at any time – sometimes changing stage with little or no warning. Sometimes companies start their ethics program at Stage 2. Sometimes companies regress, as could happen if a new CEO overlooked a company's traditional values (Stage 2) and ordered mere compliance with the law (Stage 1).

Stage 2 is values-based ethics

As companies have developed business ethics programs in recent years, something of a tug-of-war has emerged: compliance versus values – rules versus values.

Given the influence of the Sarbanes-Oxley Act of 2002, compliance seems to be winning. For example, the Ethics Officer Association (EOA) was known by that name from its founding in 1992 until an act by the board in 2005 reframed the organization's purpose by renaming it the Ethics and Compliance Officer Association (ECOA). This renaming probably was a response to 'competition' by another business ethics group, the Society of Corporate Compliance and Ethics (SCCE), a decidedly more compliance-oriented organization. While the renaming might be a wise move with respect to attracting a broader membership, a side effect is to strengthen focus on compliance. In contrast, the ethics dynamic provides good reason for values to be ascendant instead.

Some companies advance to Stage 2 whether they want to or not. Employees pull their company into Stage 2 when they recognize that rules resolve only some of their issues and concerns. Employees ask for guidance about gray areas the rules do not adequately address. Stage 2 is 'developmental' – it grows people's ability to make ethically wise decisions in a variety of circumstances that are hard to foresee. Compliance remains important, but the primary question becomes one of *values*: what is the right thing to do?

Stage 2, values, encompasses all of compliance and adds so much more that it reaches the 'next level'. This is the domain of values-based ethics, of attention to the organization's values, customs and culture, and thus it is the logical focus for managers dedicated to making their company's contribution to customers and society meaningful. The community surrounding a company provides both broad and specific influences. The broad influences include customs and norms of society, diversity, and globalization. Specific influences include laws and regulations that warrant protective controls within a company.

Of the two, broad influences probably are more powerful than specific ones. *The Kite Runner* is a novel by Khaled Hosseini, a physician in northern California who is a native of Kabul. He tells a story of boyhood, growing up in Kabul, and describes an old winter tradition in Afghanistan, a kite-fighting tournament. Contestants compete to cut each other's line, and the winner is the last kite flying. There are no rules, but custom is that whoever ends up with a fallen kite keeps it no matter what. 'Afghans cherish customs', said Hosseini, 'but abhor rules'.[5]

In US culture the relationship is not quite the other way around. 'Cherish' might be too emotional a word for our relationship to rules. 'Abhor' certainly does not describe our relationship to custom. But we think it is safe to say that, over the past 20 years, compliance with laws and rules has been at the top of the dance card for most business ethics programs in companies and organizations.

It is fascinating to see that we are not the only society to face the challenge of balancing the relationship between compliance (read rules) and values (read customs – the Latin root for 'customs' is 'mores', the semantic root of morals, which is related to values).

Customs are among the building blocks of culture, a reality that has acquired added significance and scrutiny in the ethics, compliance, and corporate governance world over the past few years. In fact, 'customary beliefs' are included as an element of culture in one definition that you will find in *Webster's Third New International Dictionary*.[6]

Customs characterize organizations and groups. This distinctiveness can contribute to the signature of a company or organization much more than simple adherence to laws that apply in the same way to every entity. At a US Senate hearing on February 13, 1900, in widely-quoted testimony about women's suffrage, Carrie Chapman Catt made the memorable observation that 'No written law has ever been more binding than unwritten custom supported by popular opinion'.

We find that to be true in an everyday practice or custom that we all participate in, namely use of the automated teller machine. When someone is at the ATM, virtually no one in the US has to be reminded to stand back, behind an invisible line. People do it automatically and, in fact, frown on those who don't respect that space. Why? Almost anyone will respond, 'privacy'. Privacy is such an overriding value in US society that it dictates a custom or behavior without law, regulation, or even a visible line. Frankly, customs go beyond laws and rules and give a fuller picture of what an organization really values. We ignore their important role in building and maintaining an ethical culture at our peril.

In practice, Stage 2 companies base ethics on values, a few principles that guide employees to make intelligent decisions. They are confronting head-on this central question: is an ethics program a tactic to protect a company and prepare it to defend against possible prosecution, or is it something more? Is ethics just law abidance? Or is it also leadership and employee development, systems analysis, attention to culture, mindfulness, and tacit wisdom?

Extending ethics beyond Stage 1 compliance requires a leap of faith that a respected, successful organization will emerge from a corporate culture that encourages and values observance of law, civility, respect for others, and a sense of personal responsibility for others and the organization. To some degree, a Stage 1 compliance program is like having 100,000 employees walk atop a narrow wall – sooner or later, someone will slip off. A company that really wants to be ethical must do more: it must create a values-based, high-ethics organizational culture. It's protective, like putting handrails along both sides of the path atop that wall.

A substantial body of systems theory research explains why companies' practical experience is that Stage 1 compliance *does not* work and Stage 2 values-based ethics *does*. We'll talk more about this later, but for now simply point out that business ethics is a system influenced by inputs from many sources outside the company's control. Because everything happens for a reason, the inputs do determine what outputs will happen, but the complexity of the inputs means they can never be fully known and so the system's outputs are not completely predictable – uncertainty exists. Research shows such systems are governed best by a few simple rules (Stage 2 values), not by extensive and detailed rule sets (characteristic of Stage 1).[7]

The strength of Stage 2 is that companies build effective ethics by developing a few values and striving to create an open climate that allows people to use those few values to make good decisions and behave ethically. Scenario-based training gives everyone practice in recognizing ethics issues in the workplace and using values to wisely resolve them.

The role of example is also important. Francis of Assisi's comment is germane here: 'Preach the Gospel always. If necessary, use words.' The message must be sent so employees, regardless of their level of education, feel encouragement to always do right; to not proceed – to stop! – when they sense 'that's not the way we do things around here'; to seek help to properly resolve an uncertain situation.

A weakness of Stage 2 would be focusing on values while ignoring Stage 1 laws, rules, and regulations. In many companies, uncertainty and confusion reign now due to a misleading diversion that happened because some people defined business ethics as 'compliance' on one hand or as 'values and virtues' on the other. Often the difference is described as law versus ethics or as rules versus values. Discussion of the relationship between these two elements has focused largely on their differences and the suggestion that they are alternatives to choose between. But defining 'rules' and 'values' as alternative approaches rather than a pair of essential components means that embracing one may necessarily exclude the other. The ethics dynamic makes clear that that would be wrong.

Nevertheless, four factors have reinforced the debate: (a) companies often create ethics programs because they already face costly law violations and want to comply with the law to prevent more; (b) the original 1991 version of the US Sentencing Guidelines for Organizations spoke in terms of compliance programs;[8] (c) so do stock exchange requirements; and (d) so does the *Sarbanes-Oxley Act* of 2002.

Well ... not exactly. The New York Stock Exchange (NYSE) implemented a requirement that listed companies must 'adopt and disclose' a code of business conduct and ethics, then explained that the code can focus management on areas of ethical risk and help foster a culture of honesty and accountability and contain compliance standards and procedures. It required effort 'to deal fairly' with customers, suppliers, competitors, and employees, then specified no manipulation, concealment, abuse of privileged information, misrepresentation of material facts, or other 'unfair-dealing practice'.[9]

Overall, the NYSE requirement emphasizes compliance. It could have been different. In response to an NYSE request for input, the [then] EOA recommended flexible requirements, suggesting that member companies should:

(a) create an 'effective' ethics and compliance program consistent with the US Sentencing Guidelines for Organizations (which *promotes an organizational culture* that encourages ethical conduct and a commitment to compliance with the law);

(b) designate a board committee to oversee that program; and

(c) provide periodic ethics and compliance 'orientation' to all board members.[10]

This would have emphasized fostering ethics in corporate culture without neglecting compliance.

With respect to the *Sarbanes-Oxley Act* of 2002, companies have given overwhelming emphasis and resources to implementation of Section 404, which required 'establishing and maintaining an adequate internal control structure' and assessing/testing the effectiveness of those controls — all compliance. The Act also contains Section 406, which required a code of ethics 'for senior financial officers' — standards reasonably necessary to promote (a) 'honest and ethical conduct' — integrity; (b) full disclosure of violations; and (c) compliance with rules and regulations. If legislative documents, like Vatican documents, should be read carefully to discern messages contained in style, placement and so forth, then that section arguably seems to give priority to an ethical culture (as well as compliance), at least among senior financial officers, but we observe that measures to implement Section 404 compliance controls have been so overwhelming that most people do not even know Section 406 exists.

In addition, people have several times explored creating an ISO standard for business ethics. ISO is the short, all-purpose name adopted by the International Organization for Standardization. Because the acronym for that organization would differ depending on language (IOS in English, OIN, in French), the founders of this nonprofit organization chose to use ISO as the short name in every language. 'ISO' comes from the Greek *isos*, meaning 'equal'. There is nothing wrong with industry-wide or world-wide standards, which ISO promotes. But ISO standards, by definition, are compliance-driven.

Beginning in 2008, a newly created US government standard affected companies doing business with the federal government. That standard requires such companies to promptly tell on themselves if they find fraud, conflict of interest, bribery, gratuities or false claims at their firm.[11] That clearly demonstrates a focus on compliance.

Ethics and values or rules and laws?

Emphasizing either without stressing the necessity of the other would be too simplistic and leave employees and the company vulnerable. Judge Richard P. Conaboy, the first chairman of the Federal Sentencing Commission, called business leaders' attention to this on September 7, 1995: 'You must take on the obligation to lead this effort, to be in the forefront, not only by working to ensure that your company's employees follow the law but by embracing and placing at the very top of your company's priorities the basic good citizenship values that make law abidance possible'.[12]

So, as part of governance, corporations need to establish policies and procedures that recognize and apply the ethics dynamic. Companies, managers, and individuals must go beyond the rules and establish a corporate culture that sees rules and values as ethical allies.

Stage 3 is trust

This next evolution of the ethics dynamic includes all of the values and compliance domains and keeps both important, but the primary question becomes one of 'trust'. Stage three is a natural focus for leaders. It is a strategic stage: are each decision's outcomes right for everyone? Is ethics a ground rule when big decisions are made? Has the company achieved a climate and culture allowing each employee to comfortably follow her or his own personal moral compass?

> *For we will hear, note, and believe in heart, that what you speak is in your conscience wash'd as pure as sin with baptism.*
>
> – *William Shakespeare: Henry V, Act 1, Scene 2*

Research indicates that companies and government show progress toward Stage 3. A study using hierarchical complexity theory found three public policy documents the US government published since the mid-1980s to shape US corporations' ethics scored at progressively 'higher' moral reasoning stages. By 'higher' stage, we mean not just doing more compliance, like attending to 20 rules instead of just two, but thinking about ethics in a different plane, like changing from linear logic (e.g. if in doubt, tell the truth), to systems thinking (e.g. organize managers of this company to create a climate of open communication that allows everyone to speak what they believe is the truth), to supersystems thinking (e.g.

companies in various industries should share, compare, and evaluate their ethics best practices so we all can become ethically more sophisticated and we all can learn to achieve our ethical best).[13]

Trust is a two-way street: employees and management need to trust each other. The CEO of a *Fortune* 100 company confided that he sometimes lies awake at night worrying that an ethical lapse by just one employee – and there are more than 100,000 employees in that company – will jeopardize the survival of the entire corporation. This is a perverse example of employee empowerment. In such a situation, the power of one employee is enormous.

Indeed, 15 years before, under a previous CEO, that corporation's survival was jeopardized by just five employees. Given what we know about this, not all were motivated by the best intentions. Some were, but other motivations were not so noble. Nevertheless, they tried too hard to be outstanding performers, tried too hard to get the results they thought the company expected, would not admit they could not do the job correctly in the time allotted, and therefore 'bent the rules a little'. Two of the five went to jail. The company survived by paying more than $17 million in fines and remediation (which ate *all* of the profit the company had earned from sales totaling more than $100 million!), by shutting the doors permanently on a 2,000-employee division, and by proving it had a good ethics program in place. A big corporation might have the financial wherewithal to do that; a smaller company likely would be wiped out. Either way, some people's jobs suddenly vaporize.

Companies need to build comprehensive ethics processes around the entire ethics dynamic model. The process should encompass several efforts that companies have thought of separately, such as business ethics, social responsibility, environmentalism, philanthropy and citizenship. This is not to say all of those efforts ought to be in one bucket. Their scope is broad and they may require leaders with differing education, experience, and sensibilities.

Where large corporations can afford to hire experts to handle a compliance or ethics specialty, small businesses cannot. Governance of a small business needs to focus on process that simplifies how business is conducted and prevents compliance or ethics problems from arising. Small business benefits from operating at Stage 2 or Stage 3 of the ethics dynamic. Good values prevent legal issues. Where trust exists, myriad problems simply do not arise.

Companies must comply with thousands of laws and rules today. To protect the company and employees, functional managers must teach each employee the laws and rules that are critical to successful performance of her or his job. Hence, managers must teach compliance. They should be familiar with compliance laws that generally affect the company and especially familiar with compliance laws that affect their area of work. You would expect all managers to be familiar with overtime and break rules for hourly employees, but you would expect procurement managers to be thoroughly familiar with procurement integrity regulations. Laws and rules offer basic and helpful clarity and direction to even the most motivated employees. A value we want to inspire and motivate is a pattern of regard for laws and rules as essential for mutual respect and the success of common process.

But more than that, and even if the department is embedded in a company which lacks formal ethics process, managers can promote Stage 2 values-based ethics and Stage 3 trust. They can motivate employees, inspire them if you will, to levels of integrity and virtue beyond the minimums set out in specific rules or laws. An emphasis here is on modeling behavior.

Individuals always are free to consciously act as 'law-abiding citizens'. In common parlance, describing someone as a 'law-abiding citizen' says more than the narrow meaning of the phrase. Like any expression, 'law-abiding' has a base meaning as well as layers of meaning and nuances that go beyond the base and deepen it. 'Law-abiding citizen' is not a simple statement about one act or even about a person's character. It indicates a pattern that says something about the person's goodness, sense of community responsibility, and ability to be counted upon. This suggests that the law, at its broadest, is not simply an instrument of order and protection in society, preventative and protective, but also a reaffirmation of justice and responsibility as societal values.

Failure to understand and implement the ethics dynamic is an important cause — perhaps the number-one cause — of business ethics failures. Stage 1 programs give too little help to the company, to employees of the company, and to all of us who want to be proud of our nation and its business community.

High ethics reliability organization (HERO)

At some point in the evolution of a company's business ethics program, the vision is likely to become one of flawless company ethics. Karl Weick and associates studied a similar concept they called high reliability organizations (HROs). They focused on organizations like the US Navy, where aircraft carriers are nuclear powered and potentially armed with nuclear weapons. The reliability of people and equipment must be super high because even a single failure could cause a devastating *physical* catastrophe. HROs must build processes and cultures that effectively address the enormous physical risk and make the organization safe.[14]

Following Weick's lead, what if such a concept could be applied to business ethics? Would a HERO be valid and desirable? On the face of it, a HERO would seek to avoid even one ethics failure. Such an organization would value the integrity of its people and believe even a single failure could cause a devastating *ethics* catastrophe. If that seems far-fetched, look at the Enron and Arthur Andersen companies to see the impact an ethics breach can have on business and society. A trend observed in US public policy approaches HERO standards by expecting major US corporations to avoid ethics disasters because they could be a catastrophe for both the company and the nation.

The HERO concept offers an attractive vision of great business ethics. It's the way people want to live. Ask a group, 'Does anyone here *not* want to be ethical? Does anyone here want to work for an *unethical* company?' We've had only one person raise his hand: a stalwart member of Rotary International, an organization famous for its strong ethical cornerstone called the Rotary 4-Way Test. He quickly admitted he raised his hand in jest, just to see what we would do. Would anyone seriously raise a hand if asked, 'Does anyone here *not* want to work for a HERO – a company committed to having no ethics failures?' ... Yes, actually, some people would object because they see and fear a downside.

A downside of the HERO concept – a risk – is the specter of perfectionism. Taken to an extreme, any mistake would evoke blame and punishment. People don't like that environment and prefer companies that encourage ethics-without-punishment, pursuing excellence, taking moderate risks, learning from mistakes, and avoiding blame or punishment of risk-takers.[15] At issue is this: can a company allow employees to take ethics risks?

The HERO concept emerges as realistic only if it is divorced from perfectionism. While no company can encourage or even allow employees to violate laws, employees face enough gray areas not clearly resolved by law that necessarily they must make judgment calls – and 'judgment' inherently means they are taking a risk. What the HERO concept requires is supportive, protective company processes that (a) help employees make a good decision in the first place and (b) quickly surface problems resulting from those decisions – or from any other cause – so the full resources of the company can correct them while they are still small. The HERO concept must recognize that any company will constantly face a potpourri of small errors and problems and provide processes to detect, investigate, correct, and learn from them. A true HERO is a learning organization, not a tyrant.

This reality is supported by collateral evidence developed by a taskforce appointed by the American Psychological Association (APA) to examine zero-tolerance policies developed in the 1980s to stop drug use and curtail unruly and violent behavior in schools. Those policies required severe punishment of any misbehavior and allowed no mitigation based on the student's intent, so a child caught taking aspirin for a headache was punished as severely as one spiking punch with methamphetamines. The APA recommended keeping the zero-tolerance standard but tailoring response to the specific infraction and developing interventions that will prevent violations in the first place.[16]

Leadership

A key component of a company's trust system is its leaders. They hold responsibility to build trust in their organization. Pennsylvania State University professors Linda Treviño and Michael Brown point to Arthur Andersen, the founder of the accounting firm that bore his name, as an exemplary builder of that firm's trust system. 'Think straight, talk straight' was a mantra there for years. Every employee was trained in the 'Andersen Way': strong ethics, integrity and high-quality work. Employees learned to speak the same language and share the same values.[17]

Andersen, in years gone by, personally demonstrated that integrity was more important than cash business. To a railway executive who demanded Andersen approve his financial accounts, Andersen said, 'There's not enough money in the city of Chicago to induce me to change that report.' The railway took away its business, but later filed for bankruptcy, and the situation reinforced the Andersen firm's reputation for trustworthiness. (In *Final Accounting: Ambition, Greed, and the Fall of Arthur Andersen,* Barbara Toffler explains how the Andersen company's ethical culture slipped badly in later years.[18])

Attempts to build trust popularized training courses designed to teach 'situational leadership'. Basically, situational leaders diagnose other people by the amount of direction and support they need to successfully complete their current work. Leaders and employees then openly agree on a mix of direction and support using these assumptions:[19]

- people new to a job (or task) want high direction about exactly what their manager expects them to do but bring such enthusiasm for the new work that they need little supportive encouragement from that manager;
- people who have worked a job for a while, but who are still learning it, still want high direction about what the manager expects them to do and by now have encountered surprising, discouraging difficulties so they want supportive encouragement from the manager too;
- people who have worked the job long enough to overcome the difficulties no longer want much direction about what the manager expects them to do but do want supportive encouragement indicating the manager appreciates their work; and
- people who are true masters of the job set their own high standards. They are 'craftsmen'. They thrive on independence. They need and want little or no direction or supportive encouragement from the manager.

While critics complain that no hard evidence proves that situational leadership works, managers in industry intuit that it pretty well describes 'how things work around here'. One explanation of the difference may be that critics are looking for objective evidence that employees perform their jobs better in a situational leadership environment – something very difficult to measure – and managers in industry are subjectively judging the trust that emerges from matching leader-employee expectations and behaviors based on situational leader relationships.

The ethics dynamic describes how people make business ethics work: compliance, plus values, plus trust. Values are a key component. Harvard professor Lynn Sharp Paine makes the point: '[M]any have come to regard a value system based on sound ethical principles as a foundation of *organizational* excellence'[20] [emphasis supplied]. We are speaking not just of 'ethical excellence' but of something far larger, something that determines how successful the entire organization will be.

Challenge puzzle

It has been widely praised as a 'gold standard' business ethics decision: Johnson & Johnson's (J&J) choice to recall world-wide all Extra-Strength Tylenol capsules on store shelves or already sold to customers. The reason was that police had notified J&J that seven people died in separate incidents in the Chicago area, apparently from ingesting Tylenol capsules containing cyanide.

No law required J&J to recall the Tylenol and the cost to the company would be more than $100 million. In fact, the FBI asked J&J to do nothing because recalling the product could give copycats reason to do similar crimes in the future. But in a very short time, J&J considered the situation and decided to recall the Tylenol because their number one corporate value was 'responsibility to doctors, nurses and patients, to mothers and fathers and all others who use our products and services'. Jim Burke, J&J CEO at the time, said 'there really was only one decision'. The basic tenet of medicine is 'do no harm'. People trusted Tylenol but people had died taking the product. 'We needed it to get off the shelves. It was the right thing to do.'[21]

Meanwhile, roundly criticized as a bad decision was Ford Motor Co.'s choice to build and sell the Pinto automobile despite discovery that its fuel tank often ruptured in a rear-end collision. Studs protruding from the rear of the axle housing punctured the tank and the fuel filler neck sometimes ripped. Spilled gasoline could ignite.

No law required Ford to fix the problem. Several modifications were possible, but all added $11 or more to the cost of manufacturing each car and therefore conflicted with a goal that total cost of the car must not exceed $2,000. Ford studied the issue for years and used a cost-benefit analysis approved by a US government agency, the National Highway Traffic Safety Administration (NHTSA), to calculate that making the $11 fix would cost $137 million and only prevent an estimated 180 deaths (each life valued at $200,000) and 180 burn injuries (each injury valued at $67,000) and 2,100 burned cars (each car valued at $700), for a total benefit of $49.53 million. Ford chose not to fix the gas tank problem.

Years later, the NHTSA formally determined that the Pinto was defective and Ford recalled the cars. Ford also was indicted for reckless homicide after three teenage girls died in a fire after a rear-end collision – reportedly the first time a corporation was tried for alleged *criminal* conduct – but was found not guilty by the jury.[22]

Laws didn't resolve the issues facing either J&J or Ford. It's a puzzle: act on values like J&J did, or act on a carefully studied, rational decision like Ford did? How can a company decide which to do?

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