

ETHICS

Ethical misconduct: Is it your biggest risk?

This article forms part of a presentation Annie Searle made early in November 2012 at the Pacific Northwest Enterprise Risk Forum

I owned a computer hardware company for 15 years, and one of my earliest writing projects was the creation of an employee handbook that outlined issues that ranged from dress code to values and acceptable behaviour. My experience of owning and operating the company offered direct, hands-on operational risk management for both myself and our customers. My ten years of experience at Washington Mutual offered a wider pathway to an understanding of all types on internal controls that are at the heart of enterprise risk management, as well as some brutal lessons on just how difficult it is to manage risk when a company is siloed and when executives cast a blind eye in order to obtain profits. My subsequent work as a consultant for critical infrastructure companies has broadened my understanding

of regulations and controls in both the public and private sector: operational risk management must be married to the strategic planning process if it is to be truly effective.

I subscribe to Basel's understanding of the factors that can lead to financial loss – people, processes, systems, and external events. Of all four, from at least what I have seen, people are at the heart of operational risk management, whether policies and programs are in effect or not. And that gets us back to a discussion of values and behaviour.

Ethics are the moral principles of right and wrong that govern conduct and illuminate character. One's character is defined by one's values. Our values and some patterns of behaviour are formed early. How old were you when a parent or teacher said "Honesty is the best policy?" How old were you when you first heard the Golden Rule: "Do unto others as you would have done unto you?" For business author Robert Maxwell, it's the Golden Rule that asks "How would I like to be treated in this situation?" He believes that question is as valid in business as it is in private life, that there should be no distinction between personal and business ethics (John C. Maxwell, *There's No Such Thing as "Business" Ethics*. New York: Warner Business Books, 2003). For the philosopher Immanuel Kant, it boils down to what Kant called the principle of publicity: "Could you stand the heat if this were made public?" Kant's question is strikingly similar to one of the filters that Nordstrom CEO Blake Nordstrom says the company applies when making a complex decision involving



ANNIE SEARLE

Annie Searle is Principal of Annie Searle & Associates LLC – also known as ASA Risk Consultants – an operational risk consulting and research firm that provides independent risk assessments and roadmaps for critical U.S. infrastructure sectors like banking and finance.

Prior to founding ASA in 2009, Searle spent ten years at Washington Mutual Bank (WaMu) where for most of those years, she was responsible on a company-wide level for business continuity, disaster recovery, technology risk and compliance, technology change management, and (for several years) for vendor and application security.

www.anniesearle.com

“Nothing can possibly be conceived in the world, or even out of it, which can be called good, without qualification, except a good will. Intelligence, wit, judgment and the other talents of the mind, however they may be named, or courage, resolution, perseverance, as qualities of temperament, are undoubtedly good and desirable in many respects; but these gifts of nature may also become extremely bad and mischievous if the will which is to make use of them, and which, therefore, constitutes what is called character is not good.”

Immanuel Kant,
“The Metaphysics of Morals,” 1797



customer, culture and reputation: “would it put us on '60 Minutes?” (for those not familiar with the American television program, it is not a program on which most companies wish to appear, since its focus is primarily investigative, shedding light on unethical or fraudulent business practices).

For many of us, ethics can be equated with doing what we say, with mirroring in our behaviour the values we espouse. In today's business environment, that can be trickier than we think. Moral trade-offs seem sometimes to have become the norm.

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Here's a selected list of CEOs removed from their positions for one or more of the seven categories of Basel risk:

- 2008** Board member and former McKinsey CEO Raj Gupta (insider trading)
- 2010** British Petroleum CEO Tony Hayward (external event)
- 2010** Hewlett Packard CEO Mark Hurd (falsifying reports)
- 2012** Highmark CEO Kenneth Melani (junior employee)
- 2012** Best Buy CEO Brian Dunn (personal misconduct)



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2010 Lotus CEO Dany Bahar (financial mismanagement)

What I understand least is how any of these CEOs did not understand Kant's principle of publicity: how did they think they would not be caught? Did they feel they were above the controls structure? On one hand, they seemed to understand how powerful they were – if they understood that, then why behave so foolishly as to get caught. Of this list, only Raj Gupta will go jail in addition to paying a large fine.

In our consulting practice, one of the first pieces of due diligence we perform is to discover whether or not a code of ethics is in place, and well-understood by employees; and whether new employees receive an orientation on corporate values and ethical behaviour.

The Risk Universe has devoted more column inches than any other publication to human behaviour and operational risk questions. In particular, the "Unethical and illegal practices rife, says survey" article (*The*

Risk Universe, July 2012) that focused on the Labaton Sucharow study and the "Whistleblowing retaliation is rising" article (*The Risk Universe*, September 2012) indicate clearly that we are not on the same page where ethical conduct is concerned; and that without some new type of training, we should decrease our expectations that employees or executives will "do the right thing."

A new study shows how much better companies perform financially when they have focused programs to identify unethical behaviour and correct it. The Corporate Executive Board (CEB) RiskClarity Corporate Integrity Service shows that, on ten year shareholder returns, higher integrity companies outperform others by 16.2%. Over 525,000 employees at 130 companies have participated in this survey that identifies seven attributes that affect corporate culture, like tone at the top, openness of communications and organisational justice.

[Click here for more information and to see the survey](#)

What specific, practical steps can be taken to improve internal programs and reduce ethical misconduct?

1 REVIEW THE CORPORATE VALUES/ VISION STATEMENT

Is it a marketing slogan, directed at customers and investors, or is it a statement of values, written to be intelligible to employees and pointing to desirable behaviour? Companies like Nordstrom and Starbucks have embedded their corporate values in front line employee behaviour.

2 CREATE/REVIEW THE CODE OF CONDUCT

Sometime ethics boils down to deciding what to do when there isn't an absolute rule or regulation. Sometimes ethics boils down to reporting misconduct rather than taking the low road. Simply following the regulations sets a very low bar. Use the values statement and the code of conduct to put a real communications program together that uses examples of appropriate and inappropriate behaviour. Make it more



than a one-time orientation with an annual online check-in.

3 INCENT EMPLOYEES TO DO THE RIGHT THING

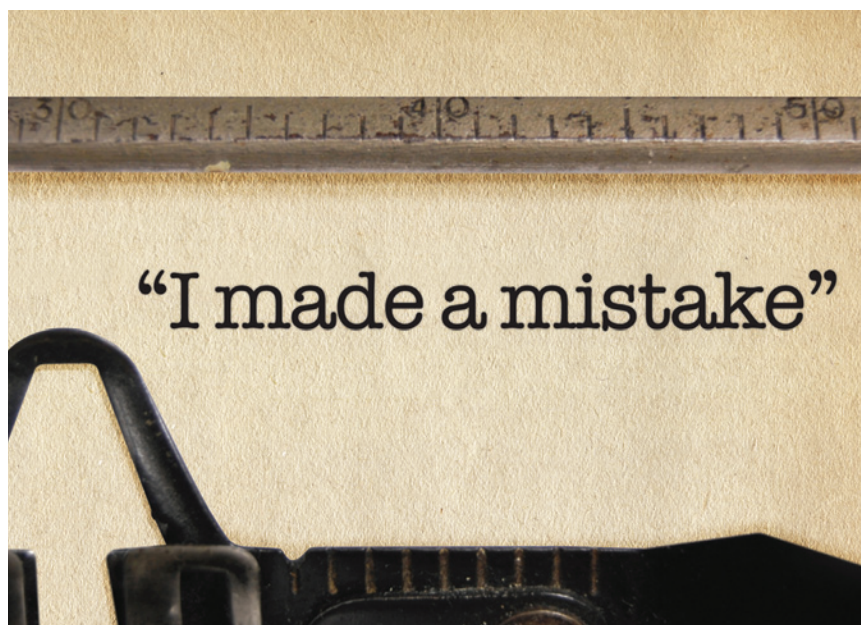
Recognise exemplary conduct. Storytelling is an effective way to make the ethical point – find employees who did the right thing even when there was no specific rule to follow or someone watching. Periodically recognise teams who perform well. Include ethical conduct as a percentage of bonus annually, either at the individual or group level. And be sure that HR profiles managers inclined to retaliate against employees who report misconduct. If they cannot correct their own retaliatory behaviour, they should not be managing people.

4 BUILD A FRAUD AND MISCONDUCT PLAN

Conduct a misconduct risk assessment. Identify weaknesses and create a mitigation plan as well as a response team. Train employees on how to report misconduct or fraud by identifying what it is. Develop a program that includes triggers to move a report from an “allegation” to an “investigation.” Make clear to staff and managers that retaliation from reporting is unacceptable in every way.

5 CREATE YOUR OWN PROGRAM

The revised SEC whistleblower program assumes that with stronger cash incentives, there will be a higher level of participation. But why not create your own program and reduce your own reputational risk directly? An internal whistleblower program that guarantees anonymity, employment protection and a monetary award is a best practice. Consider also what I call, for lack of a better term, an “I Made A Mistake” program that allows employees to self-report unethical decisions or behaviour without being punished or retaliated against. I believe there could be a lot of room here for building such a program’s requirements and scope. It is worth considering, even if the first year only brings reports of pilfered office supplies. If you deploy online training, then use lots of scenarios and multiple choice options.



Above all, you can create a climate for your team to ensure that members are not afraid to give you bad news. You can learn to say “I was wrong” and “thanks for your insight”

6 ASK YOUR SENIOR LEADERS TO REINFORCE ETHICAL CONDUCT VERBALLY AND WITH THEIR OWN PERFORMANCES

If your leaders aren’t behaving in an exemplary fashion and modeling the behaviour they wish to see from employees, it’s hard for employees to take ethics issues seriously. In this respect, misconduct by leaders could include cutting corners, manufacturing data, waiving requirements or eliminating critical risk practices.

It is fear that drives employees to misconduct – agrievement that they are not appreciated, fear that they will not get their bonus, fear that they will not be promoted, fear that they will not have enough money, and, in today’s climate, fear that they will be fired. As a leader, what else can you do? Above all, you can create a climate for your team to ensure that members are not afraid to give you bad news. You can learn to say “I was wrong” and “thanks for your insight.” This is not exactly the same as ensuring that you never retaliate against an employee who reports misconduct, but it is close. To succeed as a leader yourself, you need to remove as many of these fears as you can, to unleash as much productivity as possible, and to make it possible, through the climate you create for employees, to take well managed risks that will pay off for the company. **TRU**