Global Future Council
on Transparency and
Anti-Corruption

Good Intentions, Bad Outcomes?

How Organizations Can Make the Leap from Box-Ticking Compliance to Building a Culture of Integrity

AGENDA FOR
BUSINESS INTEGRITY

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Contents

1 Introduction

Regulators often tend to reward aggressive anti-corruption enforcement within companies. But evidence is mounting that sanctioning individuals is not enough: to thrive in the long run, companies need to build a culture of integrity. Any such effort needs to start from the recognition that many employees are well-intentioned and are simply struggling to navigate grey ethical lines. This paper, which focuses on Pillar 2 of the Agenda for Business Integrity of the Global Future Council on Transparency and Anti-Corruption, explains how companies can encourage their employees to apply ethical reasoning in the complex dilemmas all businesses face.

1.1 Overview and context

“It is extremely important to encourage people to speak up, not just in response to unethical behaviour, but to help companies identify and respond to integrity challenges before it is too late.

A remarkable expansion of the corporate compliance and ethics function has taken place over the past two decades. Strong international consensus on the critical components of a corporate anti-corruption compliance programme has emerged over the same period. Today, there is broad acceptance that a credible anti-corruption programme must include:[1]

– Senior leadership commitment or “tone at the top”
– Policies and procedures
– Risk assessment
– Third-party due diligence
– Employee training
– Reporting and investigation
– Responsible investing
– Periodic review
– Disciplinary measures

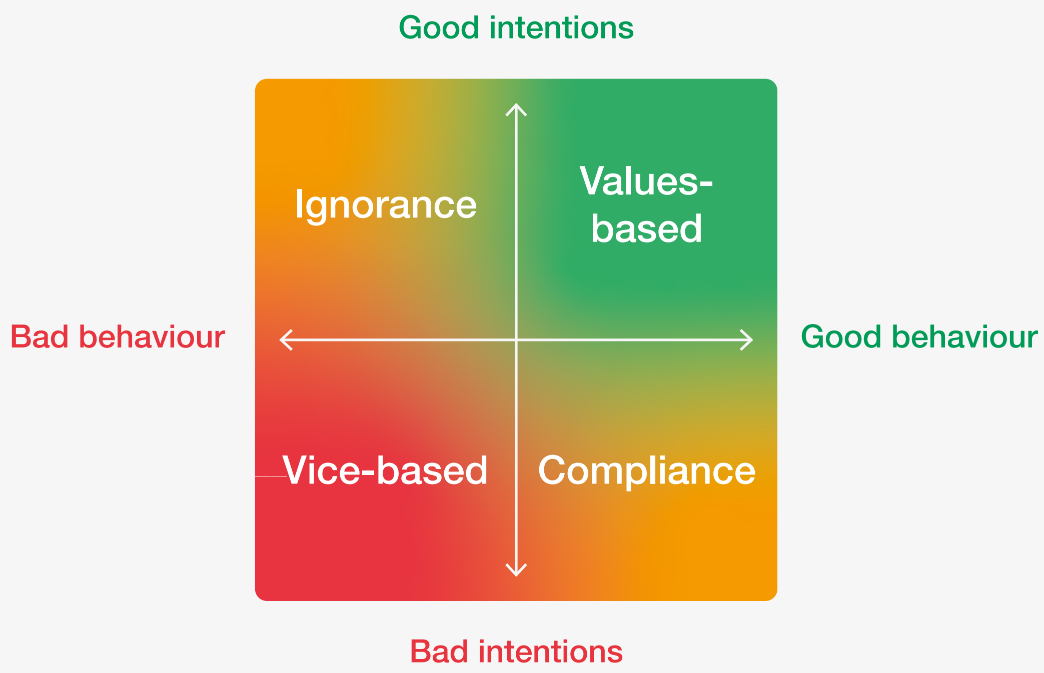
Despite the widespread adoption of anti-corruption compliance programmes with all these features, however, corporate corruption and integrity scandals are still common. Therefore, the dominant approach to anti-corruption compliance, whereby effort is focused on identifying and sanctioning individuals with unethical intent, is becoming less credible in the face of evidence that systemic corruption and fraud have taken root in a range of large multinational organizations that had established compliance systems.

As the understanding of how employees respond to compliance processes has grown, businesses, regulators and their advisers have increasingly turned their attention to how key dimensions of corporate culture, such as values, leadership,[2] norms and incentives, might support or undermine commitments to transparency and anti-corruption.

Norm generation and the creation of an ethical culture via the “tone at the top” have since been explicit goals for most corporate compliance programmes.[3] However, most compliance teams still focus on policies and processes to drive ethical employee behaviour. As regulatory implementation has advanced, regulators have tended to seek and reward examples of aggressive enforcement inside companies. As a paper persuasively argues, the consequences of this shift have been mixed.[4] Compliance teams have gained visibility and resources. But, in many cases, the compliance team has come to be seen as an internalized law enforcement body that responds to external pressure from government regulators and the public. Case in point, it tends to be staffed by lawyers – particularly, former prosecutors. This perception can have negative, unintended consequences and might even encourage employees to rationalize and justify unethical behaviour.

The simple matrix in Figure 1 illustrates why even best-practice compliance programmes, while essential, are not sufficient to drive corporate integrity. In broad terms, people’s *behaviour* can be assessed as either good or bad. More difficult, but also critical, is to assess their *intentions* as either good or bad. This, in itself, demonstrates that compliance has a limited role: it mostly tries to prevent people with bad intentions from doing bad things – in other words, finding and removing the “bad apples”. But many employees are well-intentioned and simply struggling to navigate ethical grey areas, competitive pressures and mixed messages and incentives from their employers. In some circumstances, people with good intentions engage in unethical behaviour, either because of ignorance or peer pressure, or because they are incentivized to respond to rigid rules, rather than encouraged to apply ethical reasoning and judgement to the real and complex dilemmas that all businesses face.[5] That is why more nuanced discussions about integrity and human behaviour should also be part of the agenda. It is extremely important to encourage people to speak up, not just in response to unethical behaviour, but to help companies identify and respond to integrity challenges before it is too late.[6]

FIGURE 1 | The distinction between behaviour and intentions



Source: Global Future Council on Transparency and Anti-Corruption member Daniel Malan. The design has been adapted for this report

How corporate culture is created and changed remains an elusive, complex question, and its measurement subject to intense debate and some confusion. Any culture is determined by the interaction of systems, norms and values. Much is implicit, unspoken or even unconscious among its members, making it difficult for them to identify when they might be swimming in cool water, or when they might be like frogs slowly boiling to death. The realities of power and hierarchy also generate employee concerns over performance evaluation and job security, adding to the challenges of achieving a speak-up environment and ensuring the accuracy of evaluation tools. Extensive academic literature[7] from behavioural science and organizational and social psychology might help corporations design more ethical and effective cultures, although their adoption to date appears relatively limited.[8] Companies seem hesitant to experiment with and test promising new approaches due to conformity, risk aversion and fear of regulatory exposure. However, a number of intersecting trends suggest a new imperative to focus on incentives and culture. This paper shares key concepts that might help to advance beyond tick-box compliance programmes, towards true cultures of integrity in corporations. Organizational culture is part of Pillar 2 of the Global Future Council on Transparency and Anti-Corruption's Agenda for Business Integrity.

2 Building an ethical culture

Creating and sustaining a strong ethical culture is the key to creating an organization that makes behaving ethically as easy as possible. This approach considers ethics as an organizational design issue, rather than as a series of measures to identify and sanction individual misconduct.

Many forces and factors lead people to take ethical shortcuts. But when all relevant organizational systems, processes and norms are consistently promulgating ethical conduct, ethical failure is much less likely.

2.1 Recognizing individual ethics and cognitive biases

Emerging best practice from companies suggests that incentives based on ethical conduct or social responsibility can be very effective.

Most of today's anti-corruption programmes are designed and executed with the implicit assumption that finding and removing "bad apple" or "rogue" employees is sufficient to reduce the organization's exposure to ethical risk. But this approach ignores the overwhelming importance of social context in shaping human behaviour. Although people do have different levels of personal integrity, everyone is susceptible to environmental influences. In fact, all of us have great difficulty in seeing our own ethical failures as clearly as we see those of others. A great majority of people believe themselves to be more ethical than average, which is a statistical impossibility. We all have ethical blind spots and cognitive biases and use motivated reasoning, where we are inclined to create justifications for our own behaviour – though not the behaviour of others. A weight of evidence suggests that humans will cheat a little bit if the circumstances arise – though not so much that their personal sense of morality is threatened.

With an enhanced understanding of the importance of social context, corporate leaders can increase the effectiveness of their ethics and compliance programmes as follows:

Train employees to recognize cognitive biases: Most anti-corruption training programmes focus on building familiarity with the professional, legal and reputational consequences of getting caught in a regulatory breach. Such training assumes that individual employees are making rational cost–benefit calculations about whether to engage in bribery and corruption, and are avoiding wrongdoing only when the cost outweighs the benefit. However, helping employees to develop awareness of how biases and blind spots develop is a far more useful approach in building an understanding of how corrupt practices become institutionalized. Rules and processes cannot be developed for every eventuality, and attempts to short-circuit employees' own ethical reasoning often backfire. Overall, it is more important – and effective – to equip employees with tools to help them optimize their own decision-making and build ethical awareness. In parallel, building understanding[9] of the role of time and hierarchical pressure, isolation and anxiety in undermining ethical behaviour can help employees identify when they are straying into dangerous territory and encourage them to ask for help.

Understand the role of incentives: How businesses incentivize and reward employees is one of the most critical factors determining whether they will behave ethically. It is common to find that employees are incentivized *both* to avoid compliance violations and accompanying sanctions *and* to respond to high sales targets or bonus schemes that reward achieving results by any means necessary, encourage short-term thinking and prioritize individual competitiveness over group cooperation. The problematic side effects of overprescribed goal-setting have been well documented.[10] Sales-based compensation targets set without regard to local market conditions are considered to be a particular red flag for corruption, but many companies have been slow to avoid altering their incentive structures, apparently from fear of competitive disadvantage and the superficial attraction of objective metric-driven approaches when assessing peer-to-peer performance.

Emerging best practice from companies, including Novartis, Mars and Royal Dutch Shell,[11] suggests that incentives based on ethical conduct or social responsibility can be very effective, particularly at the senior executive level, though they must be given sufficient weight in the overall incentive structure. Best-practice governance systems specify clear roles for both compliance and Human Resources in building incentives. Without a direct role in influencing incentive structures, the reach and impact of compliance programmes will be limited to isolated rules and processes that do not consider the totality of the ways employee behaviour is rewarded and sanctioned, both formally and informally, and culture is built.

Build psychological safety: An extensive study by Google Inc. found that psychological safety was the key distinguishing factor among its highest performing teams.[12] The ability of employees to take risks without fear of humiliation and punishment drives creativity, inclusion and productivity. It also vastly increases the possibility that employees will feel secure enough to raise ethical concerns without fear of retaliation or punishment. Employees often refrain from reporting ethical concerns because they believe that speaking up will not be welcomed by the organization and will evoke no response – particularly if it challenges organizational hierarchy, or there is a risk of being victimized (even where the organization explicitly prohibits such behaviour). And indeed, many recent corporate scandals have demonstrated that whistle-blowers are often ignored or even scapegoated.

The level of psychological safety is also a critical indicator of whether a team is likely to be subject to unethical behaviour. Cultures of urgency and necessity, where employees believe they face overwhelming competitive pressure and need to meet rigid deadlines, must demonstrate "commercial" decision-making as a valued attribute. This exposes employees and organizations to vastly elevated corruption risk, as such conditions are used to justify the undermining of commitments to ethics and compliance. For example, at Siemens AG, former executives said they believed that paying bribes was necessary to maintain contracts and jobs:[13] "We thought we had to do it. Otherwise we'd ruin the company." Leaders can build psychological safety about ethics in organizations by making it "something we talk about", and acknowledging complex grey areas and the need to weigh the ethical risks presented by unrealistic commercial goals. This is more effective than reducing ethical conduct to adherence to prescriptive rules and laws that cannot govern every situation nor guide the exercise of integrity and judgement as skills.

Design "nudges": Richard Thaler and Cass Sunstein's seminal book *Nudge* shows how contextual influences can be deployed to improve individual decision-making. Their findings have been used extensively[14] in the public sector for a range of goals, including improving the pension system and combating obesity. In the private sector, one of the best known and widely cited findings is that employees are more inclined to observe the requirements of a code of conduct if they sign it before – not after – they read it. Other studies have found that putting healthy food choices at the front of the cafeteria line improves eating habits. There is room for more extensive applications of nudges to encourage ethical and effective cultures in today's corporations.

2.2 Designing a more holistic approach to organizational ethics and leadership

In addition to helping individual employees to recognize and act on ethical risk, and designing incentive structures to reduce the risk of unethical behaviour, organizations can improve ethical culture if they consider the impact of strategic priorities, leadership conduct, the design of oversight systems, and the value of stakeholder trust. A more holistic assessment of the organizational culture can help us understand why compliance efforts succeed or fail, and to change the organizational context to reduce the propensity for corruption, fraud and other unethical conduct.[15] However, the benefits are not limited to the identification and prevention of wrongdoing. Ethical cultures also foster mutual trust and innovation, both of which are necessary preconditions to be able to survive and thrive – and which require diverse and inclusive perspectives and ideas. Finally, businesses in this era of COVID-19 are all experiencing new competitive dynamics, geopolitical and regulatory uncertainty, and shifting employee values and perceptions. Our working environments are becoming more fluid and intangible,[16] and the efficacy of top-down control is sharply reduced in this context.

Build a new vision for Boards: Ultimately, the challenges facing companies today require a new vision for Board oversight, which includes a far more integrated and holistic approach to ethics. An extensive white paper describes how Boards can execute on the vision of stakeholder capitalism via a more integrated approach to governance.[17] This includes a long-term vision for value creation, a more holistic and systemic approach to risk, integrated financial reporting,[18] efforts to build diversity, and active endeavours to build fair and efficient markets, respect for human rights and the functioning rule of law. This vision can be executed internationally, despite wide divergence in corporate governance structures and frameworks. It is critical to a new vision that recognizes that companies can no longer treat their impacts as "externalities", but are a critical actor in the societies in which they operate.

Improve organizational oversight: If senior leadership can successfully build a new integrated governance vision, measures then need to be taken to reflect this vision in management and oversight structures. The status and effectiveness of groups that conduct oversight, manage risk and set ethical direction are critical in driving the positive impact of any efforts at culture change – but this process is becoming more challenging. As already described, it is no longer sufficient to manage governance, risk and compliance solely via a focus on detecting illegal conduct in order to reduce regulatory risk. Ethical issues are becoming broader and more difficult to evaluate, and are increasingly converging with sustainability risks. Obvious examples include labour standards in the supply chain, carbon emissions and climate change, human rights, and employee and public activism. In 2020, many companies found that the risk of a pandemic was absent from both enterprise risk assessments and sustainability management "materiality" frameworks. Consideration of how to identify and respond to such systemic risks is essential for organizational resilience over the long term, but requires far more integration of sustainability, compliance and risk,[19] the use of tools such as scenario planning, and greater emphasis on multistakeholder collaboration to address problems that cannot be solved by any single government, company or civil society organization.

Compliance teams are better resourced than ever, but they are being asked to oversee a broader set of issues of ethical conduct and behaviour that range far beyond legal compliance. At the same time, regulations are becoming more fragmented and inconsistent across jurisdictions. This raises immediate issues of oversight and integration. Risk assessments and compliance oversight are led by specialist teams, but these teams cannot "own" ethics or individual behaviour or business decision-making. Rather, the management of ethical issues needs to be implemented throughout the business. Leading companies are exploring the effective convergence of different risk management approaches, and clearer alignment between ethics and integrity initiatives and the company's strategy and governance, with a focus on mitigating human rights and corruption risks for society in tandem with reducing legal risks for the company. Some large organizations, including Microsoft, Telenor Group, AstraZeneca, Novartis AG, Nestle and Lockheed Martin, are driving closer integration among audit, legal and sustainability functions, aligning these teams beneath a single senior executive leader.[20]

Review mission, strategy and purpose: Organizations interested in building an ethical culture focus on systems, processes and norms for good reason. However, the organization's mission, vision and core values – often described as its "purpose" – will also have a direct impact on culture. It may be stating the obvious to say that the organization's core task may support an ethical culture or may undermine it, but the impact of the core task and goals of a company can be absent from discussions on culture. In turn, this can wrongly suggest that the challenge is equivalent across organizations and industries.

There is growing evidence that managing companies with a longer-term perspective can act as a proxy for high-quality management and secure commercial success and organizational resilience,[21] compared with the consequences of an obsession with short-term value. By definition, the effective consideration of environmental, social and governance (ESG) risks often requires thinking about "long tail events" and the ultimate consequences of issues such as economic inequality and climate change on operations, strategy and competitiveness. Therefore, it is argued that any successful effort to balance long-term and short-term imperatives automatically provides the "business case" that has been the holy grail of the sustainability field for many years. How to value the consequences of systemic ESG risks, particularly where the impact is indirect, is a dynamic area of research, and many challenges remain. However, there is growing support from influential investors to reward longer-term management and governance, and this will certainly help drive more responsible business practice. For example, new research from Bank of America suggests that poor ESG performance prefigures 90% of bankruptcies.[22]

Strategic priorities matter a great deal for organizational culture. Contradictions and inconsistencies between the organization's stated values and actual priorities will be picked up by employees, affecting their behaviour and motivation – which will, in turn, affect the wider culture. Younger employees are increasingly concerned about ethical and sustainable behaviour, and increasingly willing to challenge decisions by corporate leaders that undermine commitments to ethical imperatives – internally and externally – and reward businesses with strong ESG performance by working harder, staying longer and seeking to produce better results for the organization.

Identify and encourage ethical leadership: Leaders need not be personally aware of unethical behaviour in their teams to hold some responsibility for it. The leadership of an organization integrates employees into a system via rules, norms, processes and tasks. Leaders are responsible for the strength and effectiveness of this integration mechanism, regardless of their level of knowledge of individual wrongdoing. This is the real meaning of "tone at the top", and it suggests that a focus on corporate governance, oversight and senior responsibility can yield huge benefits in terms of individual and organizational ethics.

" In an ethical culture, leaders take personal ownership of risk and are held directly accountable.

In a corrupt culture, leadership is complacent and hierarchical. It hoards information and takes care to build plausible deniability. The existence of highly hierarchical authority systems may not indicate corruption in itself, but such systems can host cultures of fear in which employees are reluctant to express concerns. By contrast, in an ethical culture, leaders take personal ownership of risk and are held directly accountable. Ethical leaders are role models, communicating the importance of ethical standards, holding their employees accountable to those standards and, most importantly, designing positive working environments for their employees. Ethical leadership has been shown to drive a host of positive outcomes and to reduce the risk of many negative outcomes. Leadership may therefore be the single most important lever in a system designed to support ethical conduct.

Increase organizational diversity and inclusion: Considerable research suggests that more diverse teams make better, smarter decisions.[23] Diverse teams are more creative and diligent.[24] To take just one example, gender diversity on Boards reduces risk-taking and improves dialogue and ethical decision-making.[25] However, it is less clear that using quotas to improve diversity statistics will be successful in isolation. From an ethical culture standpoint, a culture of inclusion is critical in enabling employees to feel comfortable to speak up and raise concerns, as well as reducing the cognitive dissonance that results when personal identity and organizational identity are misaligned.

Approaches that enable employees to have difficult conversations, manage values conflicts and speak up when problems arise should help to counter peer pressure and power dynamics, and to encourage a more open and inclusive culture. However, the onus should not be entirely on the individual employee to drive this. Leaders need to create the conditions for inclusion, which means driving psychological safety, encouraging open dialogue and enabling a sense of agency and empowerment among employees.

Measure stakeholder trust: Third-party due diligence checks are considered a must-have in any good compliance programme. Regulators emphasize the need to ensure that they are risk-based and proportionate. Still, thorough due diligence, particularly in markets that lack robust public records (most) and across all the global languages, remains a complex, expensive process marked by methodological and practical limitations.[26] (Notwithstanding improvements in both automated diligence tools and overall corporate transparency, a cost-effective approach to determine beneficial ownership is far from being a reality, to cite just one example.) It might be more effective – and easier – to complement due diligence with assessments of the level of stakeholder trust in an organization,[27] not least because stakeholder engagement is already a critical component of any credible human rights assessment. It may seem obvious that companies that pay bribes are also likely to violate labour or environmental standards, but the link between ethics and voluntary corporate responsibility efforts is too rarely recognized in compliance assessments. Over time, employees acquire a deep, implicit sense of whether their organization treats its suppliers, customers and other stakeholders with respect. They tend to know if it effectively “lives its values”, particularly when no one is looking, and respond accordingly. Stakeholder trust is therefore a promising indicator of how meaningfully a company implements its stated values and commitments.

3 Conclusion: The way forward

There are encouraging signs that corporations are beginning to understand the overwhelming importance of organizational culture in developing more effective and impactful anti-corruption compliance programmes. However, practical applications of the rich findings from behavioural ethics and organizational psychology are still disappointingly limited, despite a preponderance of evidence that these approaches would improve ethical conduct, drive organizational success and help tackle the systemic drivers of corruption. Growing interest from financial regulators in understanding how culture drives risky employee behaviour is an encouraging sign, but fear of sanctions and punishment still dominate and stymie the application of academic findings. However, at the dawn of the 2020s, many companies face unprecedented challenges as a result of younger workers who are focused on ethics and sustainability, the pressures of a hyper-transparent environment, a new focus on abuse of power in the workplace as a result of social movements like #MeToo, and the growth of political protest and employee activism. For companies that choose to address these challenges via a focus on strategy, ethical leadership, thoughtful incentives and consideration of stakeholder interests, the rewards will be rich – and sustainable.

Appendix: Global Future Council on Transparency and Anti-Corruption 2019-2020

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