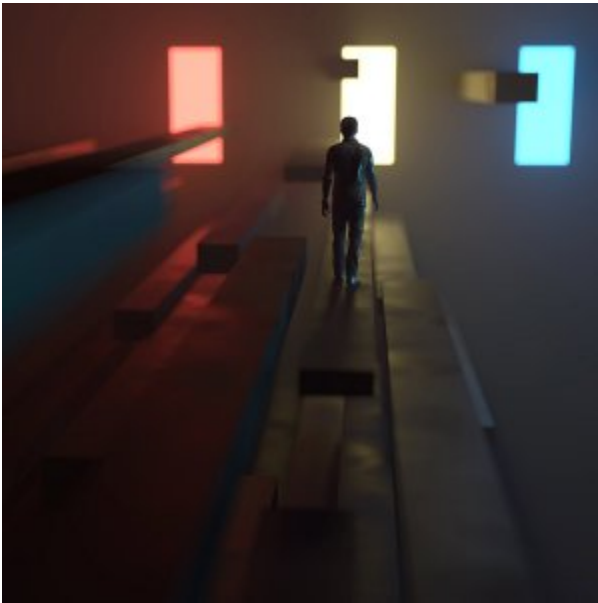# Creating an Ethically Strong Organization

CATHERINE BAILEY AND AMANDA SHANTZ

Ensuring that all employees clearly understand appropriate ways to address daily ethical issues can prevent your company from spiraling into corporate scandal.

When German car manufacturer Volkswagen was caught cheating on its diesel emissions testing regime a few years ago, the subsequent scandal launched numerous lawsuits, cost billions of dollars in fines, and severely harmed the company's reputation. The actions — and inaction — of dozens of employees at all levels, across divisions and countries, contributed to this disaster, including the software engineers who designed the cheating device, the workers who installed it, the managers who approved the fitting and testing, and the members of the senior leadership team who either orchestrated the scam or simply turned a blind eye. [1]

Of course, VW isn't an isolated example. Consider the costly lapses in judgment at Wells Fargo, [2] for instance, and at Samsung Electronics. [3] Why do such scandals continue, despite the clear moral and financial imperatives for ethical action? And — perhaps more important — what can be done to change matters?

Although some argue that people are innately inclined to behave unethically out of self-interest, [4] our research reveals that organizational ethics matter significantly to most employees and managers, and that people want to work for employers whose values and principles are aligned with their own. This suggests that ethical employers are likely to attract and retain ethical employees. [5] What's more, research has shown a link between ethical leadership and task performance, organizational citizenship, and other productive work behaviors [6] — companies have many compelling reasons to address ethical failings at the earliest opportunity. The urgency is all the greater in this digital age, since businesses must continually make rapid, high-stakes choices about how to handle sensitive customer and employee data.

To uncover the reasons behind persistent unethical conduct, we asked employees at five U.K. organizations — a national government department, a nationwide retailer, a nonprofit in the social services sector, a county-level police force, and a construction company — to tell us about their experiences of both ethical and unethical practices on the part of their colleagues, line managers, and senior executives. [7] (See "About the Research.") We found that the ethical tone of an organization is the cumulative outcome of how its members address daily ethical dilemmas as they go about their work. Over time, a consistent mishandling of these micro-level issues can spiral into macro-level corporate scandal. Here, we discuss several murky areas that employees must navigate and ways that organizations can help them make ethical choices day to day.

About the Research

To inform our study design, we carried out a detailed analysis of research over the past 25 years on ethical leadership and decision-making. We then surveyed a representative sample of 1,319 workers in the United Kingdom and conducted in-depth case studies in five U.K. organizations: a central government department with 18,000 employees, a nationwide retailer with 31,000 employees, a nonprofit in the social services sector with 1,100 permanent and 300 temporary staffers, a police force of 3,000 officers plus civilian staffers, and a construction company with 6,900 employees.

In four of the organizations, we surveyed 1,033 employees and their 524 line managers. Across all five, we conducted 46 face-to-face interviews, held 16 focus groups with a total of 79 participants, and analyzed company documentation such as human resources policies and statements of mission, vision, and values.

Daily Dilemmas That Trip People Up

When employees don't have a shared understanding of events that unfold around them, what constitutes an ethical response, and the consequences of behaving otherwise, it often means the organization has created an ethically weak situation for them. People essentially become free agents, behaving idiosyncratically in the absence of clear, strong norms. (An ethically strong situation, in contrast, is one in which "the right thing to do" is clearly communicated to employees and people have the motivation and ability to behave in ways that are consistent with the organization's ethical code. [8]) In the case of VW, an ethically weak situation was allowed to develop over many years, as senior executives prioritized market share over environmental and legal concerns in one judgment call after another.

Here are the daily dilemmas we found that tend to muddy the ethical waters for individuals in decisions both large and small.

Ethical disconnect. Sometimes employees observe a gap between their personal ethics and those of the wider organization, and that makes them uneasy. An abundance of studies show that people want to fit in at work [9] — but it's not just a fit with the requirements of the job or even a fit with the organization's culture that matters. New research is beginning to show that people have a strong desire to gain a sense of moral fit as well. [10]

Because they feel this deep-seated need, they're desperate to close the gap between their own ethics and those of

their organization. When they struggle to do so, they often withdraw and may quit their jobs altogether. One manager told us, "I've worked in businesses that I didn't stay in very long because of the ethics and the culture. I didn't feel comfortable." This sentiment is echoed by many.

Conflicting stakeholder needs. Every organization has a range of stakeholders affected by its decisions, including employees, suppliers, clients, senior managers, the local community, wider society, and even the environment. [11] Organizations may have an explicit approach to balancing these competing needs — but that may not be the same as the implicit approach that employees witness every day.

When we asked employees and their leaders to rank the order in which stakeholders "matter" in important decisions, consensus was rare. As one employee in the retail sector said, "Even though we've got a vision and we've got an ethical policy framework, I personally feel very strongly that [in practice] it's shareholder, company, colleague, in that order."

When groups of stakeholders lobby for special treatment, the situation becomes even more complex. For the nonprofit we studied, a core challenge was figuring out how to handle large donations that are linked to requests for preferential care of the donors' relatives. One manager told us, "Sometimes, the choices we have to make are not overtly compromising, but they can make things difficult — people asking for access to services when they're not entitled to them, or people jumping the queue." Managers must weigh the monetary worth of the donation against the nonprofit's values of integrity, fairness, and transparency.

While the nonprofit solved this dilemma by refusing to provide preferential treatment in exchange for donations, situations vary, and what is right for one organization may not be right for another. Even different departments within the same organization face competing priorities when having to choose between stakeholder groups. However, each time an employee or a leader makes a decision that implicitly or explicitly favors one stakeholder group over another, it sends a message to other employees about what really matters — and whose interests the organization is willing to sacrifice.

Not knowing whether (or how) to speak up. Witnessing unethical conduct by a colleague or superior forces people to decide: Do I take this further? If so, how? And what will be the consequences for me and for others?

Often, whether or not people challenge unethical behavior depends on the nature of the infraction, the setting within which it takes place, the seniority and roles of those involved, and the potential risks of challenging the behavior. Some ethical breaches are especially difficult to challenge; in many cases, staff may be unwilling to challenge upward. One government manager seemed to have realized this, saying, "I'm quite an outspoken person, and nobody has ever challenged my behavior, even though in some circumstances I recognize that I perhaps go a bit too far."

Possible responses include staying silent, taking the individual aside and discussing the matter privately, calling the person out in front of others, reporting the matter to senior staff, or reporting it anonymously via a whistle-blowing or anti-harassment program.

Some employees we spoke with described instances when they chose to stay silent. Discussing an event when

bonuses were awarded to everyone except the hourly workers on the front line, one retail employee said:

It did feel desperately uncomfortable, but in the end you either rise up as a whole population and say, "No, this isn't right, none of us are taking bonuses," or you become an outlier and a single person saying, "I don't want my bonus, I'm going to give it to charity," or you say nothing. I didn't say anything.

And a junior police officer told us:

If you and I were constables and I'd seen you behave in an unethical way and challenged you about it, that could cause bad feeling. But then if you and I went out and faced somebody going crazy with a knife, I'd need to know you'd have my back. It's not like working in an office. You

might be relying on that person to save your life.

When employees choose to stay quiet — even with good intentions — alternate viewpoints are silenced, levels of engagement and commitment are likely to diminish,[12] and others note that failure to challenge is the norm.

Conversely, in the construction company, an employee was comfortable publicly challenging a colleague for the use of sexist language; when the perpetrator apologized immediately, the interaction sent a positive message to others about how to handle such situations.

Ethics versus expediency. Another challenge is deciding what to do when the ethical solution to a problem is not the expedient solution — often because there aren't enough hours, dollars, or people to make the ethical solution happen. As one retail manager put it:

I think our ethics as a business are very, very good. Where we get the frustration is when we want to do the right thing with our people, but actually the resource levels that we're asked to work on make it impossible sometimes.
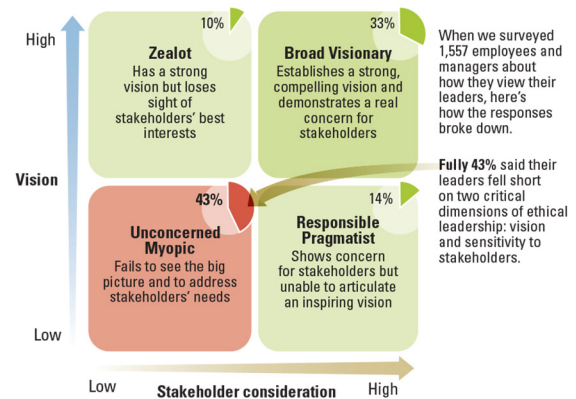
In the context of the police, this kind of problem meant that officers had to make choices about which crimes to investigate, causing "a huge amount of strain and stress to officers because they can't do the job they're trained to do, that they're paid to do, that they want to do, and is the reason why they joined in the first place," according to a leading officer on the force.

Two Critical Elements of Ethical Leadership

The number of CEOs sacked for ethical misconduct has risen 36% in the last five years, [i] including such high-profile examples as Yahoo CEO Scott Thompson, United CEO Jeff Smisek, and LendingClub founder Renaud Laplanche. But the problem of unethical behavior can't be "solved" simply by firing senior leaders who behave badly.

To bring about lasting change, organizations must invest in "distributed" ethical leadership. That is, they must hire and cultivate leaders at all levels who promote ethical behavior. Two essential ingredients are a strong vision and a deep commitment to stakeholders.

Our research shows that employees who see their managers as ethical leaders are more satisfied with their work, are more willing to go the extra mile, find the work that they carry out has significance in the broader scheme of things, and are less likely to quit. Unfortunately, most organizations aren't poised to reap those rewards.

When we surveyed 1,557 employees and managers about how they view their leaders, here's how the responses broke down.

Fully 43% said their leaders fell short on two critical dimensions of ethical leadership: vision and sensitivity to stakeholders.

Zealot (10%) — Has a strong vision but loses sight of stakeholders' best interests

Broad Visionary (33%) — Establishes a strong, compelling vision and demonstrates a real concern for stakeholders

Unconcerned Myopic (43%) — Fails to see the big picture and to address stakeholders' needs

Responsible Pragmatist (14%) — Shows concern for stakeholders but unable to articulate an inspiring vision

Axes: Vision (High / Low); Stakeholder consideration (Low / High)

Call to Action

No organization is free of these dilemmas, but they can be managed. Our research and analysis suggest that the following six steps can help leaders set an ethically strong tone so that employees are better equipped to make the right choices day to day.

1. Acknowledge ethical ambiguity. Many organizations do not recognize or discuss ethically tricky situations their managers and employees face. This drives individuals to internalize their decision-making processes — which can create a slippery slope.

In the police force we studied, even though leading officers were well aware that budget cuts meant increased workloads and longer hours for the rank and file, they had not openly acknowledged these pressures with their staff and how they might affect day-to-day decision-making — preventing an authentic dialogue about the problems or possible solutions. One leading officer said, "We are really struggling, and we're not admitting that to people on the ground." Officers and staff felt the pressure but, given the lack of open discussion, assumed that senior leaders did not care.

In organizations with a culture of transparency, people are more inclined to seek to understand the underlying rationale for decisions. This has a positive effect on ethical decision-making because values are exposed when they are openly discussed rather than inferred from town hall meetings or company documentation. At the nonprofit we studied, one executive noted: "You know, I've worked for places where things are done behind closed doors and you don't really understand the reasons. I think here, whatever initiatives are being run, it's done very openly. We don't make decisions in hiding; we make decisions in a very consultative way." So when its employees wonder how, for instance, to respond to a donor who requests a service, it's easier for them to make that call, because they have a clear understanding of the organization's ethical values and are confident they can go to their managers for clarification or support without fear of being negatively judged.

2. Clarify the ethical trade-offs. Another important step is to explicitly clarify how employees should balance the needs of different stakeholder groups.

Most decisions will affect more than one set of stakeholders. Although the needs of all groups can sometimes be met, trade-offs are usually necessary. When employees are not sure how to manage this tension, unethical approaches can develop.

In the retail company, leaders paid lip service to meeting customers' needs above all others, but their behavior wasn't always consistent with that message, which created confusion. Employees reported that decision-making was more often governed by immediate profit considerations and key performance indicators. Some felt a degree of cynicism toward the company's "customer first" rhetoric,

believing that in practice senior executives were more concerned about hitting performance and sales targets by persuading customers to buy add-on products and services than about caring for the customer or providing excellent customer service. One employee said: "You always have that tagline at the end, 'The customer comes first,' but at the end of the day it's a business and the people at the top know we need to hit a KPI figure."

Confusion about whose needs to prioritize can be compounded when an organization has been through a series of mergers or takeovers that bring together different ethical climates. In these cases, leaders have an especially significant role in establishing a consistent ethical framework and guidelines for balancing stakeholder interests.

Providing employees with a clear statement of vision can help them weigh competing concerns and make appropriate trade-offs. In the police force, for instance, a widely shared "Plan on a Page" helped officers understand policing priorities (such as child abuse and exploitation, modern slavery, and violence) and provided guidance on serving the needs of the community (by putting the victim first and communicating effectively with the public) while also making the most efficient use of resources.

3. Ensure role-modeling from the C-suite down. Employees observe how leaders actually handle ethical dilemmas, rather than what they say about ethics, and will infer the organization's real priorities accordingly. VW is a case in point: Though senior executives claimed to care about "clean diesel," they apparently both condoned deliberate cheating on emissions tests and encouraged employees to hide or destroy its evidence. [13]

When the senior team sends mixed ethical signals, mid-level managers may pick and choose what to follow. These mixed signals cascade through each level of the organization. As one employee in the construction business said, "If your direct line manager isn't setting an example for you, it detracts from the message that the business is giving."

We did find that the ethical conduct of mid-level managers can compensate for mixed messages from the C-suite, slowing or even reversing the development of an ethically weak situation. In the retail business, for example, the staff talked positively of the "family atmosphere" and shared values within individual stores and regions that counteracted the dominant "cost control" messages from the head office. However, a much more reliable approach is to set the desired example at the top. The nonprofit fostered an ethically strong situation by clearly showing how core ethical dilemmas should be resolved: When a company bidding to work with it asked one of the nonprofit's trustees to put in a good word for it, its leaders immediately ruled out the company as a partner due to a misalignment of ethical values.

4. Embed ethics in corporate policies and programs.

Ethically strong situations are developed in settings with robust codes of conduct and policies for enforcing those codes. [14] Such policies should include clear rules about bullying, harassment, and whistle-blowing. And they should be conveyed and reinforced through on-boarding, leadership development, and other training programs.

Without formalized policies around ethics, efforts to create an ethically strong situation will most likely founder. As one police officer said, they "help people understand why we need to behave, act, do things in a

certain way, and what the consequences are for *not* doing that."

Although corporate policies and programs alone will not eliminate unethical practices, [15] their existence is essential. For example, at the nonprofit we examined, employees were frequently confronted with ethical dilemmas when working with clients, such as how to assess mental capacity or how to manage end-of-life issues and determine appropriate levels of treatment and support. The organization helps its employees make ethical decisions by developing clear policies on approaches to care and providing training that specifically focuses on such challenges.

Similarly, at the construction company, part of the recruitment process involves matching applicants' ethical values with those of the business. It has also adopted a code of conduct and a formal framework called "What Good Looks Like" to guide employee behavior. Training on topics such as how to deal with anti-competition risks and health and safety issues is compulsory for line managers, and an online system allows for logging any health and safety issues as they arise. Although employees sometimes feel that these processes slow decision-making, they provide clarity and "consistency, and people know what is expected of them," according to a front-line manager.

5. Empower individuals to handle ethical breaches.

Ethical breaches will inevitably arise, of course — whether through error, neglect, or deliberate action. But ethically strong organizations explicitly say how people should deal with them when they do occur, in addition to trying to prevent them in the first place. Employees at all levels then feel more empowered — and obliged — to call

out bad behavior, even when doing so may be difficult. For example, employees in the construction company are required to challenge decisions and actions that could compromise the health and safety of employees and customers alike. One manager said that the culture around this is so strong that "in extreme circumstances, people have lost their jobs because they haven't followed through on what really is their duty to either challenge it there and then or report it later to make sure remedial action can be put in place."

In ethically weak organizations, challenging people's behavior is not the norm. Sometimes employees fear retribution, because they do not see others around them raising questions. Or they may feel that no action will be taken if they do speak up. [16] Sadly, that assumption isn't necessarily unfounded. While some VW employees apparently did challenge the use of "defeat devices" designed to cheat the emissions tests, their concerns were ignored. [17] So far, the evidence suggests that more than 40 VW employees in different roles and at varying levels of seniority were implicated in the diesel emissions scandal. [18] Had individuals felt empowered to challenge ethical breaches, perhaps the scandal could have been contained before erupting on such a massive scale.

6. Embrace a higher cause. Finally, ethically strong situations are characterized by the presence of a transcendent cause that unites the organization behind a vision and set of values that go beyond self-interest. One employee called this "the vision that brings you back tomorrow."

The nonprofit's transcendent cause is to provide care and support for the community; for the police, it is to keep the community safe from harm. The construction company's ethical vision of sustainability translates into protecting the environment as well as safeguarding its employees and customers. As one of its managers told us, "A lot of practices in our industry do create harm for the planet, and so we're trying to reduce our CO_2 emissions."

When a company's mission or vision is unclear or divorced from ethics, or, as a senior leader at the retail organization said, when "the 'why' is missing" altogether, an opportunity to provide guidance is lost and an ethically weak situation develops. But an overarching sense of purpose creates a context within which micro-level ethical dilemmas can be resolved.

Conclusion

Setting the stage for ethical behavior isn't just a top-down exercise — though clear direction and positive role-modeling from senior executives do help. Organizations must also consider the daily ethical dilemmas that their managers and employees face and give them the tools to make good choices. This involves regularly checking in to ensure that codes of conduct are clearly articulated and upheld — and imposing consequences when they are not.

No company is immune from ethically questionable decision-making. But by openly acknowledging and carefully managing murky situations that come up again and again, organizations become much less susceptible to egregious lapses in judgment — and less likely to incur the associated reputational and financial costs.

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