Chapter 4

Codes of ethics

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'As the adoption of corporate codes becomes the norm, the incidence of insincere, rhetoric-based codes never designed to move beyond a cursory treatment of issues... is likely to increase.' (Erwin 2011)

All Western industrialised countries have introduced legislation and guidelines to strengthen corporate governance practices and reduce corporate fraud. In response, organisations are ever more developing and presenting codes of ethics (CoEs) as 'evidence' of their regulatory compliance and to help protect those who hold responsible positions in listed companies from subjection to profound penalties, including – should things go 'wrong' – lengthy prison sentences. (Helin & Sandström 2010; Singh 2011; McKinney *et al*. 2010; Welsh 2007)

For example, the Australian Stock Exchange's (ASX) Good Corporate Governance Principles and Recommendations (ASX 2010) requires companies to develop and disclose a code of conduct, with listing rules that require the company's annual report to state the extent to which the company complies with the recommendations. Also, CoEs are '... usually regarded as the most important component of an ethics program.' (Kaptein 2011, p. 246)

Regrettably however, CoEs are widely regarded and reported to be ineffective (Singh 2011; Kaptein 2011; Erwin 2011; Kaptein 2010; Helin & Sandström 2010; Kaptein 2009; Kaptein & Schwartz 2008). Based on a review of the literature into the development, implementation and effectiveness of CoEs, this chapter attempts to explain why most codes are ineffective and provides recommendations on how – through involving staff in their development – codes can be made more effective.

[1] This article builds on Bowden, P & Smythe, V 2008. Making Codes of Ethics Meaningful and Effective. *Keeping Good Companies.* November ed. Sydney: Chartered Secretaries Australia Ltd.

Code of ethics or code of conduct?

A code that gets its hands dirty identifies and applies itself to practical ethical issues and behaviour and is often called a code of conduct. By its nature it is more useful than a 'hands-off' values statement or more idealised or aspirationally styled code of ethics. The research findings presented in this chapter show that codes of ethics are on the whole ineffective and that one of the main reasons for their ineffectualness is that they tend not to address the real ethical problems specific to the organisation, industry or profession. Supported by that evidence, this chapter recommends codes of ethics be designed to describe and deal with the concrete moral challenges that code users are likely to encounter at work and outlines what the organisation or profession recommends as acceptable ways to resolve those ethical dilemmas. Therefore, in this chapter the term code of ethics includes codes of conduct, business codes of ethics, and statements of values and ideals that are intended to cover those new or unanticipated ethical difficulties that an employee may encounter.

There are two clear reasons behind the reported ineffectiveness of CoEs: they are used as public relations vehicles, and they are used more to constrain and control staff than to govern and improve the ethical behaviour of the organisation as a whole.

Vapid codes

This first species of code are those that are commonly perceived to be mere window-dressing (McKendall *et al*. 2002; Brytting 1997; Adams & Emmelhainze 1999; Kalk and van Tulder 2001; Pagnattaro & Peirce 2007; Weaver *et al*. 1999; Jovanovic & Wood 2007; Collen 2002; Barry & Stansbury 2007; Singh 2011). These codes appear to be written to convince customers, suppliers, employees and shareholders that the company is honest and trustworthy. Behind such codes, however, there is rarely any substantial managerial back-up to ensure that the code is ethically useful and relevant to the needs of the organisation and its stakeholders.

Enron Corporation's CoE is perhaps the best known example of just such a public relations exercise. A 64 page document, bulging with nebulous platitudes, it represents a hallmark in corporate hypocrisy and is quoted on several internet sites. One site quotes Enron's Chairman, the late Kenneth Lay, convicted[2] on ten counts of conspiracy, securities and wire fraud in the corporate trial, and of all charges against him in his personal banking trial:

> 'As officers of Enron Corp, its subsidiaries, and its affiliated companies, we are responsible for conducting the business affairs of the companies in accordance with all applicable laws and in a moral and honest manner...We want to be proud of Enron and to know that it enjoys a reputation for fairness and honesty and that it is respected.' (Enron 2000, cited on Soxfirst)

The site adds 'For a company whose name has become a byword for corruption, the document makes extraordinary reading' (Soxfirst 2006). Furthermore, the Enron CoE prohibited directors, officers or employees from trading in Enron stock, an issue on which several of Enron's directors came unstuck. Backed by the above example, it seems

[2] Kenneth Lay died soon after his conviction and all charges against him were then dropped.

unnecessary to provide further explanation as to why staff regard such codes with much scepticism.

Codes to constrain

This second category contains codes that staff regard as top-down management dictates, designed more to protect the organisation by prohibiting, for example, employees' theft and misuse of the company's resources than to support the organisation's ethos as a whole. Research published in 2000 into codes used by Australian companies, in comparison with other international codes found that most Australian corporate codes were directed towards internal, rather than external issues and were designed to stop actions by staff that may have been detrimental to the organisation (Wood 2000). With a collection of over 850 CoEs of professional societies, corporations, government and academic institutions gathered over twenty years, The Illinois Institute of Technology's examination of codes describes them as 'controversial documents' (IIoT 2009).

Despite there being little or no evidence to show that CoEs prevent or reduce unethical behaviour (Kaptein 2011; Erwin 2011; Helin & Sandström 2010; Kaptein & Schwartz 2008), organisations continue to place increasing reliance on COEs as a tool with which to restrain and control staff or to capture the benefits that accrue to organisations that behave ethically.

This myth, that CoEs can be used as a tool to control unethical behaviour, pervades code literature. Critics of studies into the effectiveness of codes have concluded; most research that attempts to analyse code outputs (rather than content or how they are communicated) shares a common focus on establishing how codes may or may not influence behaviour (Helin & Sandström 2007). For example, 'codes can be effective instruments for shaping ethical behaviour and guiding employee decision making' (Stevens 2008: 601). However, of the eight studies Stevens tabled as evidence of code effectiveness[3], Kaptein and Schwartz interpreted the results of four of those studies quite differently: the Somers (2001) study, they say, produced 'mixed results'; the Schwartz (2001) study 'provided only weak correlation'; the Adam and Rachman-Moore (2004) study also provided only mixed results; and the Trevino and Weaver book (2003) is not a study of codes but 'an example of how many

[3] Stevens analysed these eight studies: Somers, M J 2001. Ethical Codes of Conduct and Organisational Context: A Study of the Relationship between Codes of Conduct and Employee Behaviour and Organisational Values. *Journal of Business Ethics,* 30, 185-195, Fisher, C. 2001. Managers' Perceptions of Ethical Codes: dialectics and dynamics. *Business Ethics: A European Review,* 10, 145-156, Trevino, L K & Weaver, D. 2003. *Managing Ethics in Organisations,* Stanford, Stanford University Press, Chonko, L B, Wotruba, T R & Loe, T 2003. Ethics Codes Familiarity and Usefulness: Views on Idealist and Revalationist Managers under Conditions of Turbulence. *Journal of Business Ethics,* 42, 237-252, Schwartz, M 2001. The Nature of the Relationship between Corporate Codes of Ethics and Behaviour. *Journal of Business Ethics,* 32, 247-262, Adam, M A & Rachman-Moore, D 2004. The Methods Used to Implement an Ethical Code of Conduct and Employee Ettitudes. *Journal of Business Ethics,* 54, 225-244, O'dwyer, B & Madden, G 2006. Ethical Codes of Conduct in Irish Companies: A Survey of Code Content and Enforcement Proceedures. *Journal of Business Ethics,* 63, 217-236, Vitell, S J & Encarnacion, R H 2006. The impact of corporate ethical values and enforcement of ethical codes on the perceived importance of ethics in business: A comparison of U.S. and Spanish managers'. *Journal of Business Ethics,* 64, 31-43.

scholars suggest... that organisations can steer the conduct of employees to only a limited degree'. From their meta-analysis of 79 empirical studies of code effectiveness Kaptein and Schwartz concluded that 'the results are clearly mixed' (Kaptein & Schwartz 2008: p.113). They explain that the 'misleading' conclusions produced by many studies into code efficacy are due largely to the significant challenges when attempting to measure code effectiveness.

The most difficult of these challenges is that a great many studies do not identify what the objectives of the codes they study are meant to be. Some codes make it clear that they aim to reduce child labour, enhance corporate reputation, reduce fraud, or increase diversity, and so on. But many codes present only vague aims, so their effectiveness *cannot* be measured. Varying definitions of key terms also form part of the larger problem of questionable research methods, therefore, sound knowledge of code efficacy remains elusive (Kaptein & Schwartz 2008). Another meta-analysis of 38 empirical studies drew similar conclusions – that studies represent a mixed image of the effectiveness of corporate codes of ethics (CCEs) and there still seems to be some uncertainty about whether CCEs lead to more ethical behaviour (Helin & Sandström 2007). At that stage little research had been conducted into how codes are developed and communicated or what to overcome when implementing a code. As Kaptein and Schwartz stated:

> 'To date, there is no empirical study which relates the impact of the code to the process in which the code has been developed and/or updated.' (Kaptein & Schwartz 2008: p.119)

The importance of development, content, communication and embedment

Until 2011 there was a gap in the empirical evidence to support any one process of code development and adoption over another. But the field of research has deepened. The factors that most influence the effectiveness of codes of ethics are being unearthed and the quality of code content, the ways in which codes are developed, communicated and embedded are being studied and compared to the ethical performance of organisations.

Empirical research relating the ethical performance of organisations to code quality makes it clear that it is not enough to merely *have* a CoE (Erwin 2011) – the ways that a code is developed and communicated are vital to its success. The Erwin study compares the quality of CoEs from 392 international companies with their CSR performance. The measure of code quality was taken from the Ethisphere Institutes[4] code quality rankings. Data from five CSR ranking agencies was used to determine an overall measure of CSR performance for each company.

Although Erwin advises: 'The practical implication of these findings to businesses is clear: high quality codes of conduct are more effective in guiding employee behavior and establishing a more socially responsible organisational culture.' But he summarises the results of his study with: 1. variability within code quality may impact code effectiveness,

[4] http://ethisphere.com/

thus potentially skewing studies that compare companies based (solely) on code presence or absence; 2. high quality codes are correlated with high CSR (corporate social responsibility) performance, although *causality of this relationship is uncertain* (emphasis added); and 3. low quality codes do not necessitate low CSR performance (Erwin 2011).

Understandably, the integrity of the process that feeds a code's development affects the quality of the finished code and, as the results of Erwin's study show, a high quality code *can* correlate with a high corporate social responsibility (CSR) ranking. Yet, just as smoke cannot cause fire, even a high quality code alone is not enough to extract ethical behaviour from individuals within the company or from the company itself – the work that goes into producing the code is as important as the code itself and companies that put sincere effort into developing a high quality code also tend to elicit more ethical behaviour from the organisation (Erwin 2011).

The Erwin study supports the intuitively appealing link between high code quality and high CSR performance (Erwin 2011). It also supports the central message of this chapter – that *how* a code is developed is what matters – because the term *quality*, as Erwin defines it for his study, bundles the discrete processes of *how* a code is developed, communicated and reinforced, with *what content* results from those processes. 'Although quantified primarily based on code content, 'code quality' is defined herein as *inclusive of code development and content...* (emphasis added) due to the close link and overlap among these steps[5]... in the code formulation process.' (Erwin 2011). Within his definition Erwin captures the nub of this chapter: the processes of code development and embedment are entwined with the quality of content and subsequent efficacy of a code. As Kaptein recites, '...the process of developing BCEs (business code of ethics) is important in creating support for it, improving awareness, and stimulating a sense of ownership.' (Behrman 1988; Stead *et al*. 1990; Webley 1988 cited in Kaptein 2011).

Muel Kaptein produced the first empirical study to test simultaneously the impact of *content*, *communication* and *embeddedness* on the effectiveness of business CoEs (Kaptein 2011). Building on over a decade of research (Kaptein & Wempe 1998; Kaptein 2004; Kaptein & Schwartz 2008; Kaptein 2010; Kaptein 2009), Kaptein hypothesised and tested five factors: code content, communication frequency, communication quality, embedment of the code by senior managers and embedment by local managers. The results of this study show that the most important of the factors he tested is how well business CoEs are embedded in the organisation by both senior and local management (Kaptein 2011). Given this, management may be interested in one study that tested the embeddedness of codes of ethics and provides a model of areas to consider when implementing and monitoring a code of ethics (Svensson *et al*. 2011).

Reasons to develop an effective code of ethics

This chapter began by pointing to a reason to develop an effective CoE; the legislation, guidelines and penalties that most developed economies have in place requiring and recommending the use of CoEs to buttress corporate governance practices. This section

[5] See the appendix A for detail on the Ethisphere method of ranking code quality.

outlines the Australian requirements and provides further research-based reasons to develop a high quality CoE.

In the final months of his tenure as chairman of the Australian Competition and Consumer Commission (ACCC), Allan Fels introduced policies to reduce penalties in light of corporate compliance with the Trade Practices Act. More changes followed. These were revisions in 2004 to the Corporations Act (2001), the introduction of the AS 8000 series of Australian Corporate Governance Standards including the Australian Standard on Organisational Codes of Conduct: AS 8003-2003. In 2007 the Australian Stock Exchange (ASX) Council released its Corporate Governance Principles and Recommendations, now in its 2nd edition[6] (ASX 2010).

The content of the Corporations Act and ASX Corporate Governance Principles and Recommendations may eventually be strengthened to the level of the US Sarbanes-Oxley Act which is more rigorous than Australian legislative requirements. Introduced following the WorldCom and Enron debacles, Sarbanes-Oxley legislates board responsibility, the establishment of ethical standards and a CoE, and the creation of an internal whistleblower system, thus providing a more potent atmosphere for ethical business than we have in Australia.

But adherence to rules and guidelines alone, however, could deliver a somewhat rigid morality, in which 'right' and 'wrong' are predominantly dictated by an outside force[7] rather than as one's conscience, character or consideration might demand. Developing an ethos might entail more than following rules. The Chartered Secretaries of Australia Good Governance Guide expresses it thus: 'A code of ethics expresses fundamental principles that provide guidance in cases where no specific rule is in place or where matters are unclear.'(CSA 2010, p.1)

So although the regulatory pressure to develop a code of ethics is considerable, researchers have identified more positive reasons that might encourage refurbishment of an ineffective CoE. Results of extensive surveys of employee attitudes indicate that most of us want to work for an ethical employer (Valentine *et al*. 2011). Also, staff believe that an ethical company will treat them more fairly and will itself behave toward the outside world in ways that elicit greater trust in management, loyalty to the company, job satisfaction, creativity and productivity, and much lower rates of reported intentions to quit the company (Fleischman & Valentine 2008; Valentine *et al*. 2011; Mulki *et al*. 2006; Jaramillo *et al*. 2008). Lower staff turnover alone flows into longer retention of experience and intellectual capital and reduced training costs. Companies with stronger corporate social performance (CSP) also tend to produce better corporate financial performance (CFP) (Orlitzky *et al*. 2003)[8]. Orlitzky's subsequent summary of the empirical evidence to date concludes that the data is clear – the idea that there is a trade off between CSP and CFP is a 'false dichotomy' (Orlitzky 2005, p. 50). The view that corporate social performance is a cost only is 'obviously wrong... CSP is effective (in terms of financial benefits for the organisation) because a firm's reputation is important with investors, analysts,

[6] See the appendix B for the ASX recommended content of a CoE.

[7] I.e. stage four (law and order morality) of Lawrence Kohlberg's six stages of moral development.

[8] Winner of the 2004 Moskowitz award for outstanding quantitative research relevant to the social investment field. The Moskowitz Prize is awarded each year to the research paper that best meets the following criteria: 1. practical significance to practitioners of socially responsible investing, 2. appropriateness and rigor of quantitative methods and 3. novelty of results.

researchers, business teachers, consumers, current and prospective employees, and other stakeholders.' (Orlitzky 2005, p. 50). More simply, such primary benefits are accumulated by companies that align their products with the ethical values of consumers (Erwin 2011). In 1970 Milton Friedman called CSR hypocritical (Friedman 1970), but societies have since changed. CSR is today firmly in line with what consumers expect. From the literature and empirical evidence it is clear – there is a positive correlation between corporate social and financial performance. 'Good Ethics is Good Business' and those who continue to disagree refer to outdated material (Beurden and Gossling 2008).[9]

Resistance to codes of ethics

Before suggesting a method of developing an effective CoE, it would be helpful to provide more detail as to why codes that constrain are on the whole ineffective. If inflicted upon staff as tools of management, there are specific ways staff can resist such codes. Understanding how and why staff might impede the adoption of a code is an important step toward understanding the importance of involving staff in the code development process.

Codes are usually produced some distance from and deposited upon those who are supposed to use them, often by the overseas parent company or upper management. Studies have shown that the closer staff can be to the making of the code, the stronger will be their sense of ownership and appreciation of the code (Kaptein & Wempe 1998; Valentine *et al*. 2011; Kaptein 2011). The degree of sense of ownership that staff hold in a company policy is crucial to how relevant they perceive the policy to be to themselves and their work. In a case study of how staff in a Swedish subsidiary of an American multinational firm resisted the parent company's CoE, Helin and Sandstrom describe and explain three modes of resistance, so effective that they found it difficult to find any signs of the parent company succeeding with implementation of the code (Helin & Sandström 2010). Local staff, when asked to read, accept and sign the code further distanced themselves from the code by adopting the mental attitude of 'not for me' or 'applies to others' – hence staff can deny the code by denying they have any involvement in the key areas the code addresses. Staff also reported that they saw themselves as separate, unique and outside of corporate power relations, and 'just wanted to get on with their work'. This, they explain, was an understandable reaction to a document perceived as a threat to individuals' innate human need for autonomy. Further distancing reactions reported were the ways staff devalued and downplayed the code's core values, or negatively anticipated the expected outputs, i.e. that the code would never lead to something good. Interestingly, Helin and Sandstom point out that although staff kept the code at a distance, they were "still dominated by the parent's demand to 'read, understand and accept' the code" (Helin & Sandström 2010 p. 597) thus rendering staff vulnerable to the disciplinary process. In this way top down CoEs disempower employees rather than facilitating more ethical behaviour.

The extent to which the problems surrounding the general ineffectuality of codes can be overcome is proportional to the quality of the processes of code *development,* quality of code *content* and depth of code *embedment*. As Helin and Sandstrom put it: 'A more participative

[9] The Beurden and Gossling literature review includes all post 1997 literature on the subject of the relationship between CSP and CFP, including 34 empirical studies.

implementation process would probably create a more active involvement [in their use of the code] among staff...' (Helin & Sandström 2010, p. 599). Similarly, institutional sustainability theory supports placing responsibility for the development of ethical policy in the hands of a group of staff members rather than solely with senior management. Development agencies use this type of approach – the involvement of participants in the decision process – to ensure commitment by recipient groups to sustain economic or social inputs.[10]

Designing a code of ethics from the ground up

Aspirationally' styled codes contain statements of values more associate with codes of ethics. Codes of conduct contain more practical guidance relating directly to the ethical issues that staff are likely to encounter in their work (CSA 2010). We advocate a mix of both in one document.

Statements of values are statements like 'be ethical', 'act with integrity' and 'be honest with customers, staff, owners and suppliers' etc. These statements can sometimes be taken to excess. The Australian Public Service (APS) Values and Code of Conduct in Practice (APSC 2009), for instance, is an 88 page document that opens with a list of fifteen values that could arguably be condensed. For example, '…The APS is apolitical, performing its functions in an impartial and professional manner' overlaps with '…The APS delivers services fairly, effectively, impartially and courteously to the Australian public and is sensitive to the diversity of the Australian public.'(APSC 2009, p2). Of the fifteen values statements, seven guide employment within the APS (merit, discrimination, internal ways of relating, equity in employment, equal opportunity, fairness and career-based) (APSC 2009). The bulk of the APS document bristles with do's and don'ts, even casting constraints as far as 'post-separation' (APSC 2009, p. 71) and the contentious arena of restraints of trade.

It is also interesting to compare previous and current versions of an organisation's CoE. The Institution of Engineers, Australia (now renamed Engineers Australia), 2000 CoE (2000) differs markedly from their 2010 release (Greyston 2010). Version two of Engineers Australia's CoE is a three page list of 30 or so remarkably short statements of values and general guidelines – some only three or four words long. For a profession that specialises in delivering the most tangible of services, their later, much shorter code, is surprisingly less applied than its predecessor. For example, the more verbose first version gives this clear guidance:

> *Members ... should not accept compensation, financial or otherwise, from more than one party for services on the same project, nor provide free services, unless the circumstances are fully disclosed to, and agreed to, by all interested parties (2000 p. 5).*

From version two, guidance on the above matters relating to compensation would, one assumes, have to be gleaned from either '...in managing perceived conflicts of interest, ensure that those conflicts are disclosed to relevant parties' (Greyston 2010, p. 2) or from 'do not engage in fraudulent, corrupt, or criminal conduct' (Greyston 2010, p. 2). From either of these statements it might not be clear to an inexperienced graduate engineer that a

[10] See for example: Lewis, D 2003. NGOs , organizational culture, and institutional sustainability. *The Annals of the American Academy of Political and Social Science,* 590, 212-242.

materials supplier's invitation to attend a 'free' 'educational' seminar at a luxury resort on the tropical island of Vanuatu should probably be politely declined.

Notable for its absence from the new version is the old code's advice to whistleblowers. Today whistleblowing policies are vital to all codes of ethics. Why, at the end of a ten year period during which all Western countries have strengthened their whistleblower legislation[11], Engineers Australia chose to remove all whistleblower guidance from their new code is questionable.

Engineers, by the very nature of their occupation tend to be pragmatic people. But the guidelines and values set out by Engineers Australia's CoE depend on abstract principles that a senior engineer, thanks to their experience, will probably already appreciate. As the 2005 National Business Ethics Survey (NBES) conducted by the Ethics Resource Center (ERC) found: 'This study also reveals that ethics training is more helpful in preparing junior level employees to handle ethics situations than senior ones.'(Choi & Seligson 2006, p. 16) and '... junior employees may need instructions on how to proceed when faced with ethics challenges.'(Choi & Seligson 2006, p. 6). What the Engineers Australia code does not provide is practical guidance to the novice who has not yet experienced the grittier ethical dilemmas that exist in engineering. Rather, junior members would be expected to act based on their individual interpretations of the '... provisions and spirit of the Code (p. 2)'.

In the following paragraphs we set out a six point program of how to develop a more useful and effective CoE:

Involvement of staff

The involvement of staff in the development of the code can help overcome the problems associated with staff regarding it as a senior management dictate. Throughout this chapter the significance of the development process in contributing to the long-term efficacy of a code and sense of code-ownership by staff has been emphasised by reference to the findings of code studies, best typified by: 'A good code corresponds to the concrete moral dilemmas which employees of the firm experience in their duties.' (Kaptein & Wempe 1998, p. 863). The research further supports our assertion that, just as people cannot be taught to be ethical, so codes cannot – and consequently ought not to be written to manipulate behaviour. Staff, given adequate support facilities to develop their own code – at times in discussion with senior management on desirable policy, and with the eventual endorsement by the CEO – will produce in an effective code for the organisation, one that is actually followed.

The process of code development should be seen as an aspect of producing an ethics training course. Developing course and code content starts with asking staff and local management to recognise the ethical challenges specific to their organisation.

The importance of the contribution of senior and local management

As described earlier, of the five factors Kaptein tested, he found the most important is how well business CoEs are embedded in the organisation by both senior and local management

[11] See chapter 3 on whistleblowing.

(Kaptein 2011; Harned *et al*. 2003; Choi & Seligson 2006). So, following on from the preceding arguments for a well-grounded code, the level of dedication by senior management is what most influences a company's ethos. One component of this commitment is symbolic, as in the CEO's endorsement of the code. Another is systemic, for example the assignment of independent staff to manage the ethics program of which the code is an integral part. But there are other ways that local and upper management can have positive influence. In the 2005 National Business Ethics Survey (NBES), the key finding was that the 'ethics related actions' (ERAs) of senior employees '... have an especially large impact on outcomes expected from an ethics and compliance program'(Choi & Seligson 2006, p. 1). Specifically, these are:

- setting a good example,
- keeping promises and commitments, and
- supporting others in adhering to ethics standards.

There will be decisions on corporate ethical behaviour that have financial implications; issues of safety training, environmental protection, gift giving and receiving, treatment of suppliers and buyers, and even shareholder policy will require executive approval. There will be times when those who are developing the code will have to mediate and reconcile differences of opinion between the company's executives.

CEO support and executive endorsement of the code, expressed in an introductory statement by the CEO or executive committee, including mention that the code was developed by employees with the full support of senior management and that what measures the organisation has adopted to ensure compliance, would be a potent statement, likely to increase the appeal of the organisation to stakeholders.

The identification of the organisation's ethical issues

The real ethical issues experienced or likely to be experienced by staff and the organisation or professional association and its policies on handling them, must be set out in the code. These issues can be identified in a number of ways – through the use of an external consultant, through interviews of a range of middle to senior management, by a search for what others in the industry have identified and through workshops – but most likely by a combination of these methods. Workshops can be designed solely to develop a code or as part of a wider ethics training program. The ethical issues could range from the relatively mundane, such as the company's policy on gift giving or receiving, to the more complex. A company working in developing countries, for instance, will often be working in an environment where bribes and extortion are normal. At times the continued operation of the business will require it to accede to what in Australia is considered an unethical demand but which is common practice in most other companies operating in that country. The company will need to decide how its own staff should respond in such ethically ambiguous situations.

Establishment of an independent whistleblower support system

ASX (ASX 2010), Secretaries Australia (CSA 2010), The Corporations Act (2001) and Standards Australia (AS8000) all recommend that companies publish a CoE containing whistleblowing provisions. A whistleblowing structure is a method by which a company

prevents retaliation toward, and provides support for, a person who exposes wrongdoing. Whistleblower support systems usually include a confidential hotline by which employees can report unethical or illegal behaviour. In most cases, the hotline does not investigate, unless authorised to do so by the company. Alternatively, the company could develop its own system but ensure it is independent.[12]

Establishment of a system of sanctions for breaches of the code

If there were no traffic police to catch and fine those who ignore traffic regulations, the number of accidents would increase dramatically. For similar reasons organisations should have a system of sanctions for code violations. Grades of sanctions should be developed, beginning with warnings, escalating to expulsion. Outside of companies, professional or trade associations can impose disciplinary sanctions on their members. But when it comes to imposing sanctions, these bodies have histories of reluctance because they fear losing members. Nevertheless, industry associations and professional societies *are* the strongest arbiters of ethical behaviour within their industry and it behoves them to apply sanctions commensurate with their responsibility.

Assignment of staff to manage the code and ethics related activities

Systems designed to build ethical behaviour in an organisation require people to develop and run them. The tasks are many, including: identifying the more serious ethical issues staff face, developing a code, implementing a whistleblowing system, defining the aims of a corporate social responsibility program (for listed companies), organising programmes to develop the new code and train current staff, and putting in place processes for training new staff. Human and financial resources should to be assigned to each of these tasks. For a small company, one person part-time may be enough. For a large corporation it may be a centralised group or individuals spread over divisions, headed by an ethics committee answerable to the Board.

Because staff tend to be more willing to talk freely to an external person than somebody they know, organisations should consider contracting outsiders to carry out interviews, facilitate workshops and research the key ethical issues. In this way staff can feel safe to contribute high quality content. Whilst consultants can organise and facilitate the project, and even the training, identification of the real ethical issues must come from within the organisation. To lighten the financial impact consultants can have, some training companies offer train-the-trainer services in which selected staff can be trained by specialist ethics trainers so that training skills, resources and knowledge flow into the company to be retained.

Conclusions

Most organisations have a code of ethics written by management as a tool with which to constrain staff or to improve the appearance of the organisation to its stakeholders. According to the research presented in this chapter, both varieties – hence the majority

[12] See chapter 3 on whistleblowing.

of codes – are ineffective at supporting the ethical behaviour of staff and the organisation as a whole. Codes of ethics are also presented to help shield those who govern listed companies from the penalties that can be imposed upon them if a court finds they have failed their legal obligation to put in place anti-corruption policies. But there are better reasons to develop an effective code of ethics: strong links have been found between the quality of codes of ethics and the ethics of company cultures, and between corporate social performance and corporate financial performance. These links have been identified, tested and confirmed by empirical studies and, for organisations that devote specific human and capital resources to developing a high quality code of ethics, the rewards will come. The most important factors influencing the quality and effectiveness of a code of ethics are the degree of staff involvement in developing the code and the depth of embedment of the code in the organisation by senior and local management.

Appendix A:

Table 4.1

Critical components used to benchmark corporate codes of conduct by the Ethisphere Institute and relative weight of each component used to calculate overall grades		
Analysis component	**Component description**	**Weight (%)**
Public availability	A code should be made readily available to all. What is the availability and ease of access to the code?	5
Tone from the top	Level at which the leadership of the organisation is visibly committed to the values and topics covered in the code.	15
Readability and tone	What is the style and tone of the language used in the document? Is it easy to read and reflective of its target audience?	20
Non-retaliation and reporting	Is there a stated and explicit non-retaliation commitment and dedicated resources available for making reports of code violation? If so, is it presented clearly?	10
Commitment and values	Does the Code embed corporate values or mission language? Does it identify the ethical commitments held to its stakeholders (e.g. customers, vendors and communities)?	10
Risk topics	Does the Code address all of the appropriate and key risk areas for the company's given industry?	20
Comprehension aids	Does the Code prove any comprehension aids (Q&As, FAQs, checklists, examples, case studies) to help employees and other stakeholders understand key concepts?	5
Presentation and style	How compelling (or difficult) is the Code to read? This depends on layout, fonts, pictures, taxonomy and structure	15

Appendix B:

Australian Stock Exchange Council's suggestions for the content of a code of conduct [13]
Box 4.1: Suggestions for the content of a code of conduct
Companies may find it useful to consider the following matters when formulating a code of conduct:
1. Give a clear commitment by the board and senior executives to the code of conduct. This is often linked to statements about the aspirations or objectives of the company, its core values and its views about the expectations of shareholders, employees, customers, suppliers, creditors, consumers and the broader community.
2. Detail the company's responsibilities to shareholders and the financial community generally. This might include reference to the company's commitment to delivering shareholder value and how it will do this, and the company's approach to accounting policies and practices and disclosure.
3. Specify the company's responsibilities to shareholders, employees, customers, suppliers, creditors, consumers and the broader community. This might include reference to standards of product quality or service, commitments to fair value, fair dealing and fair trading and the safety of goods produced.
4. Describe the company's approach to the community. This might include environmental protection policies, support for community activities and donation or sponsorship policies.
5. Articulate the company's responsibilities to the individual. This might include the company's privacy policy, and its policy on the use of privileged or confidential information.
6. Outline the company's employment practices. This might include reference to occupational health and safety, employment opportunity practices, special entitlements above the statutory minimum, employee security trading policies, training and further education support policy, practices on drug and alcohol usage and policies on outside employment.
7. Describe the company's approach to business courtesies, bribes, facilitation payments, inducements and commissions. This might include how the company regulates the giving and accepting of business courtesies and facilitation payments and prevents the offering and acceptance of bribes, inducements and commissions and the misuse of company assets and resources.
8. State the measures the company follows to promote active compliance with legislation affecting its operations wherever it operates. This might include stating whether the company's policy is to comply with Australian or local legal requirements regarding employment practices, responsibilities to the community and responsibilities to the individual, particularly if the host country follows materially different standards than those prescribed by Australian law or international protocols.
9. Specify how the company handles actual or potential conflicts of interest. This might include reference to how the company manages situations where the interest of a private individual interferes or appears to interfere with the interests of the company as a whole and how the company prevents directors, senior executives and employees from taking improper advantage of property, information or position, or opportunities arising from these, for personal gain or to compete with the company.

[13] Extract from ASX's Corporate Governance Principles and Recommendations with 2010 Amendments, 2nd edition.

10. Identify measures the company follows to encourage the reporting of unlawful or unethical behaviour and to actively promote ethical behaviour. This might include reference to how the company protects those, such as whistleblowers who report violations in good faith, and its processes for dealing with such reports.
11. Describe the means by which the company monitors and ensures compliance with its code.
Note regarding point 10 above: For guidance on the provision of a whistleblowing service, see Australian Standards on Whistleblowing Programs for Entities (AS 8004).

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