ETHICS AND THE NEW ROI

return on integrity

The latest Global Corruption Barometer reveals that almost half of South Africans have experienced bribery versus a global average of 27%. *The Trillion Dollar Scandal*, a report published by the international non-profit organisation ONE, details how Africa and other developing regions lose an estimated $1 trillion every year because of corruption. Internationally, corporate tax evasion is increasingly in the media spotlight.

The business media is full of bad news stories involving corruption, bribery and collusion. Yet, the attention devoted to the need for better ethical conduct in business is not always matched by an equivalent understanding of how business ethics can add value to an organisation. There is a sound business case for the proactive management of ethics as a strategic advantage. What's more, acting on this business case can allow organisations to access the ROI – or return on integrity – that flows from making an investment in ethics.

Understanding ethics

Virtually every employee, manager and leader has some insight into what being ethical is or looks like, or what being unethical entails. But because this insight can be subjective, organisations should ideally create a common understanding of ethics. Defining ethics as 'the right thing to do' is inadequate. A better definition would be that ethics is 'doing the right thing when no one is watching'.

Crucially, ethics involves executives and employees making choices between what is good and bad, right and wrong. Misconduct rarely results from a lack of knowledge or understanding about what is or is not right. The employee who steals from the company or solicits a bribe knows that his or her behaviour is wrong.

Therefore, ethics programmes should not simply address what employees may or may not do. Instead they should aim to influence their moral choices through all three primary drivers: leadership, values and rules (including laws, regulations and codes of conduct).

A key feature of ethical behaviour is that it impacts on others. This is encompassed in the concept of an ethical boundary. If the organisation operates within a very exclusive ethical boundary, it means that it is primarily focused on its own interests. On the other hand, an organisation with a strongly inclusive ethical boundary would incorporate the interests of relevant stakeholders and pursue a triple bottom line that adds social and environmental responsibility to profit.

Setting ethical boundaries and including the interests of others lie at the heart of expanding the purpose of business from "the business of business is business", Milton Friedman's narrow view, to "the business of business is about sustainable business".

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The significance of this shift is that business ethics have moved beyond straightforward compliance, a code of conduct, or a focus on values to include organisational purpose. Today, an organisation cannot consider its behaviour ethical unless it is actively embracing sustainability.

The business case for ethics

While understanding that ethics is a valuable and indispensable foundation, the difficult part is living the principles of ethical behaviour and acting accordingly. To achieve this, it is crucial to fully appreciate the benefits of being ethical and managing ethics effectively.

The business case for ethics rests on a strong ethical culture delivering three important outcomes: more compliance, less unethical behaviour and a minimised probability of ethical failure. Delivering these outcomes decreases the risk of consequent loss and damage. This can range from financial costs, such as fines or legal settlements, to reputational damage, eroded market confidence, a declining share price and even business closure.

Collusion by the construction industry on projects during the 2010 FIFA World Cup run-up in South Africa revealed some of these negative consequences, highlighting the way ethics can be eroded when companies focus on achieving the best possible short-term financial results. The consequent fines by South Africa's Competition Commission may not have eliminated all the profit companies made, but they damaged their reputations, while the risk of further action against individuals remains.

Another primary reason for managing ethics proactively is because it creates an environment of trust within the workplace. This brings numerous advantages, such as faster and more consistent decision-making, stronger confidence in top management, and greater individual accountability with less need for policing. A high-trust culture also enhances employee commitment and customer loyalty, supports the recruitment and retention of top talent and promotes good stakeholder relationships. In addition, a strong ethical reputation increases brand equity while making access to capital easier and cheaper.

Arguably, the ultimate benefit of proactive ethics management relates to competitive advantage. Many sources of competitive advantage have a limited lifespan because they can be copied so easily and quickly. An ethical business culture is a far more valuable source of competitive advantage because it cannot be easily copied or bought, sold, owned or traded.

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Instead, it must be built up over time and lived every day. Consequently, as the demand by stakeholders and broader society for clean business grows, this is likely to become an increasingly important business rationale for pursuing an ethical approach.

Effective ethics management

Many organisations still respond to ethics only reactively or manage ethics on an ad hoc basis, rather than adopting a proactive approach by implementing a comprehensive ethics management system. The challenge of bringing this alive was eloquently expressed by the company secretary of a large company, who posed the question: "Personally, I understand what ethics is, but what does that mean I should do in our organisation?"

▲ *See the EY Trialogue research into social and ethics committees on p.22*

In theory, this question should be answered by the organisation's social and ethics committee (SEC), as defined in the Companies Act 2008 (Act 71 of 2008). The functions which the Act assigns to the committee are to monitor the company's activities relative to social and economic development, good corporate citizenship, the environment, health and public safety, consumer relationships, and labour and employment; to draw matters to the attention of the board as required; and to report to shareholders at the company's annual general meeting. However, the Act does not provide clarity about how the company should monitor these issues.

A sound ethics management system can meet the requirements of the Act while also providing clear guidelines on the best approach to managing ethics.

Ethics are everyone's responsibility

Crucially, implementing an ethics management system involves formally assigning ethics within a company and clearly defining people's roles and responsibilities in relation to these ethics.

The social and ethics committee, as a board-appointed committee, may be the most relevant structure, unless the organisation has appointed an ethics officer in a more senior position. The company's leadership and human resources department also have a distinct role to play in managing ethics. So do the compliance, internal audit and risk functions. In fact, actively promoting and enforcing sound ethical behaviour among their employees remains a core responsibility for all managers.

The elements of an ethics management system

Ethics Monitoring & Management Services has developed a management system that comprises three foundational pillars and three action pillars.

The three foundational pillars are: **leadership commitment, ethics goals and strategy**, and **ethical standards**.

We have specifically named the pillars in this way because if any of them are absent, the effectiveness of the ethics management system would be minimised. This applies, in particular, to leadership: leaders need to commit to acting ethically and promoting ethics at all times.

These three foundational pillars support and reinforce each other. Ethics goals set the direction and define the desired outcome, while ethical standards need to be clearly defined in a code of ethics and/or a code of conduct to clarify the behavioural boundaries inside which ethics goals can be achieved. Goals and standards need to be shared among all employees.

To support its ethical objectives, a company's ethics strategy needs to incorporate a dual focus on increasing ethical conduct and decreasing misconduct. It also needs to extend beyond a limited focus on compliance. After all, simply complying and eliminating misconduct would not produce all the elements that an ethical culture stands for.

The three action pillars are: **ethical awareness**, **assessment and reporting**, and **operational ethics**.

High levels of ethical awareness not only promote ethical conduct, but are particularly effective as deterrents to unethical behaviour in the same way as visible policing is. Awareness can be built by meaningful ethics training and regular communication along with simple steps like including ethics on the agenda at management and executive meetings.

In addition, companies need to assess and report on ethics regularly, a process that builds greater awareness. Rather than a small, select sample, assessments should produce representative, quantitative results that identify and prioritise actions to improve ethics. This, in turn, allows accurate, informative ethics reporting.

The third action pillar, operational ethics, involves putting ethics into action and making them visible across the organisation's practices, systems and procedures. This can impact on many areas, including business strategy; decision-making; client/customer relations; corporate tax; procurement and supply chain management; remuneration; selection and recruitment; promotions; and gifts and hospitality.

An ethical culture is one of a company's most valuable assets and a core driver of long-term success. Long term, it ensures that companies remain compliant with less effort. It also builds trust internally and externally, increases brand value and drives more authentic sustainability efforts.

In short, a widely held and shared understanding of ethics across a company combined with genuine leadership commitment to inclusive ethics underpinned by a sound ethics management system can deliver a significant ROI – or return on integrity.

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MODEL OF THE ETHICS AND MANAGEMENT SYSTEM

This model illustrates the three foundational pillars or elements of the ethics management system at the centre, with dotted lines to indicate that they are related to and depend upon each other. The three outer action elements of the ethics management system should flow from and be based on the foundational elements. The action elements are not rigidly separate either, but interact to boost and support each other. The combination of these six pillars creates a framework for achieving the optimal goal of an ethical culture, which is accordingly positioned at the centre of the model.