CORPORATE GOVERNANCE AND ORGANIZATIONAL CULTURE. THE ROLE OF ETHICS OFFICERS.

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Abstract: We argue that ethical leadership must be in line with corporate governance in general and of the CEO (Chief Executive Officer) who must be the starting point for the rest of the organizational members to have an ethical guideline to follow. Nevertheless, we argue that the figure of the EO (Ethics Officer) is the connecting link between ethical values of Corporate Governance, CEOs and those of the other staff. With this idea in mind, we present the characteristics an EO must have, and reach the conclusion that organizational ethical values cannot be imposed. Instead, they must be managed through a *corporate governance ethical culture*, so this term will be the focus of the paper.

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Introduction

There is currently a growing concern for ethical values in the business world (which is reflected in the growing literature about this topic (1, 2, 3, 4, 5)). In any case, we run the risk of converting much of what is related to business ethics into a mere fashion if it really do not have practical value.

A large number of problems arise in this context that have to do with the creation of the EO (Ethics Officer) figure and the role he or she must play in order to champion business ethical values that can later be assumed by the rest of the organization. Indeed, the fact that the responsibility for ethical issues is delegated to a single person, who is usually not the CEO (Chief Executive Officer) or the corporate governance board in general, will be discussed in this paper.

Nevertheless, this cannot lead us to assume that the appointment of an EO is negative for the organization. In fact, this paper has as its aim to defend the validity and usefulness of this figure as long as some premises essential for its success are fulfilled. We will refer to those premises in more detail below.

Therefore, and in a summarised way, we have set three objectives for this paper:

1. Establishing the essential interrelationships between corporate governance and business ethics.
2. Determining the characteristics and specific role of the EO, taking into account that ultimately the CEO and the corporate governance board must be responsible for the ethical guideline to follow.
3. Establishing the patterns for the creation of an ethical culture through the symbolic leadership of the firm's corporate governance and the EO's actions in formal corporate ethics programs.

Organizational culture and corporate governance. Connections with business ethics

In order to achieve the first aim, we will lay the conceptual foundations of organizational culture and corporate governance, after which we will analyze how they both can be used to achieve a set of desirable ethical values that can be shared by the members of a firm.

As far as organizational culture is concerned, instead of analyzing various definitions of this expression, it makes much more sense to describe its essential characteristics. Thus, “it has a guiding role that helps to know which activities suit best the firm's personality” (6, 7, 8); “its existence is associated with the idea of sharing intentions” (9, 10, 11); “it is due to an empirical need to solve managerial problems” (12, 13, 14); and finally “it is specific to each firm” (15, 16, 17).

From all these distinctive features associated with the term “culture”, we propose the following comprehensive definition: set of values, symbols and rituals shared by the members of a specific organization, which describe the way things are done in order to solve managerial problems, both internal ones and those related to clients, suppliers and the business environment.

It must be emphasized that these values can only have a life of their own if we make sure they are shared by the vast majority of corporate members (18, 19). In other words, these values cannot be in the mind of a single executive or a small group of executives; they must be assumed by the rest of people in the organization. From this perspective, corporate governance appears as a function that can largely help to consolidate organizational behavior patterns.

Problems may arise if the previous aim is not achieved. If the senior management decides to formulate a strategy without the involvement of middle managers and others, it will have a difficult time espousing a collegial flow of authority and influence (20).

At this point, having in mind different definitions (21, 22, 23, 24), we can understand

corporate governance as the processes by which organizations are directed in a framework of legal, institutional, cultural and social factors that requires balancing the interests of various stakeholders and society.

In other terms (25), the complexity of corporate governance means that no one theory or model of society is likely to be sufficient for understanding, evaluating or designing governance structures. In a similar way, it can be said that there is little consensus on what good corporate governance entails (26).

For these reasons, if managers want to perform corporate governance, not only do they have to know the problems related to staff expectations but they also must provide solutions to those problems, which in turn will progressively consolidate their managerial position.

In this sense, the flair for communication then reveals itself as essential to perform this leadership task (27, 28).

Another aspect to have in mind is that corporate governance is not the panacea for the resolution of group or individual problems within the firm. In this respect, no leadership style can solve alone all the situations in which a manager might find himself. Emphasis will have to be laid on one aspect or another depending on the specific department or individual concerned. An essential quality for those who have to develop this function lies in being able to diagnose the specific situation and knowing which of the possible ways or styles to deal with it is the best and therefore should be chosen.

In short, leadership by corporate governance goes beyond management, since it also includes the concepts of encouragement, help and service to others with the purpose of carrying out the organizational mission through ethically correct work (29).

By relating all the above to ethics, we can provide an initial approach to the study of relationships between culture and ethics that consists in analyzing how the cultural model of a specific society can make firms located in diverse geographical areas and created according to different socio-economic postulates, share similar ethical beliefs. Interesting contributions in this respect are made by the literature (30, 31, 32, 33, 34).

It is, however, in corporate culture studies that we can best deepen our understanding of possible ways to improve organizational ethical behavior. In this sense, cultural research not only includes theoretical and epistemological issues, but also ethical ones (35); culture is more powerful than anything else in the organization (36). We can go even further saying that organizational ethical culture or, more specifically, the ethical environment within the firm

created through management practices and espoused values, may be the most important deterrent to unethical behavior (37); or also point out that behaving ethically depends on the ability to recognize that ethical issues exist, to see things from an ethical point of view. This ability to see and respond ethically may be related rather to attributes of organizational culture than to attributes of individual employees (38).

At this stage, we should clarify something important: all firms have cultures, although it cannot be inferred from this that the actions of all firms are ethically correct. There are cultures where ethical issues are denied, ignored or removed (39). Furthermore, trusting, admiring and respecting a leader do not necessarily mean that followers will behave with integrity (40, 41).

In parallel, since we are talking about ethical culture, these values must necessarily be shared with firm members and should not be only in the mind of a manager who is responsible for 'ethical issues'. Under this point of view, the ethical culture of an organization would be reflected in the beliefs about the ethics of an organization which are shared by its members (42). We can easily understand from these arguments why the literature gives so much importance to employee involvement in ethical issues related to the firm, because at the end it's a cultural matter (43, 44, 45).

From this perspective, we can say that the ethics component of organizational culture is composed of a complex interplay of formal and informal systems that can support either ethical or unethical behavior. The formal systems include leadership, structure, policies, reward systems, orientation and training programs, and decision-making processes. Informal systems include norms, heroes, rituals, language, myths, sagas, and stories (46).

Corporate Governance and Ethics Officers

A first approach for a definition of the EO is simply describing him or her as the manager whose main responsibility lies in achieving an appropriate code of organizational ethics (47). More precisely it can be pointed out that the EO is someone who makes sure the organization is doing its best to satisfy stakeholders (all those internally and externally related to the firm, such as employees, shareholders, clients, suppliers, the local community and the society as a whole) (48). As can be seen, this is 'a lot of work' for a single person.

We must also point out that the impact caused by an EO results from both a practical and symbolic dimension. We want to highlight the symbolic aspects insofar as the presence of an EO within an organization shows that the senior management is committed to ethical business

conduct (just like creating the figure of a quality manager can lead us to infer that the senior management sees quality as something important). The symbolic approach is so relevant that exists an Ethics Officer Association (<http://www.eoa.org>) with over 1000 EOs, all of them from large firms in the global field. Concerning this association, an empirical study shows that its membership is more likely to be from: at first, large firms characterised by low accounting returns and, at second, managed by CEOs who have been more recently appointed to their positions (49).

At this point, we agree with the view that “the strategic leadership of ethical behavior in business can no longer be ignored” (50).

As for the discussion about who must be responsible for ethical matters, we believe this is a function of the corporate governance in general and the CEO in particular, since the definition of the firm’s ethical values and the CEO’s conduct in relation to these values are starting points that will later become ethical guidelines to be followed by other organizational members.

From this important premise (the exercise of ethical leadership by the corporate governance), the figure of the EO when he or she carries out his or her task properly can become the meeting point between the senior management, in general, and the rest of the collaborators of the firm, as far as ethical issues are concerned. We are aware of the fact that ethical management issues are not easily delegated in the same way as production, marketing or finance functions. Nevertheless, the creation of the EO figure is justified once the ethical guidelines have been established. For this reason, as long as the senior management actions really follow those guidelines, the EO figure’s ‘diffusing’ effect can find its *raison d’être* in the organization and support leadership.

This idea allows us to describe the essential requirements an EO must fulfil, which can be summarised as follows: having a wide knowledge of the firm, mastering management techniques as well as theoretical and practical issues related to business ethics and, the same as the rest of the senior management, having the hierarchical authority necessary to exert an influence on firm members’ behavior. Not belonging directly to a functional department can be convenient too, as it confers more credibility and impartiality upon him or her. The EO should also have a good reputation and be well known by everyone in the organization.

In turn, we can summarize these characteristics saying that EOs come from diverse backgrounds such as legal matters, human resources, finance, auditing, security, or line operations, but share common characteristics such as:

1. They are strong communicators – with excellent and effective communication skills, including public speaking, presentations and one-on-one interactions with employees at all levels.
2. They are objective and thoughtful.
3. They have the ability to establish and maintain credibility and trust throughout the organization.
4. They have the ability to quickly assimilate information relating to complex issues.
5. They have the ability to network on all levels of an organization.
6. They have reached personal and professional maturity.
7. They show rationality in tense interpersonal situations.
8. They have a deep organizational knowledge.
9. They have a working knowledge of applicable laws and regulations.
10. They have experience with training and development including best practices in ethics and compliance education.
11. They have solid, broad management skills.
12. They are discreet and able to protect confidential information.
13. They are able and willing to take a difficult or unpopular position if necessary.
14. They have common sense.
15. They always show the highest integrity (51).

Of course, all these characteristics are for a “perfect person”, but as more close is the EO of them, it would be better. In our opinion, the EO figure must be carefully analyzed, as it is very risky to leave in the hands of a single person all the ethical issues associated with an organization (no matter how well this person might fulfill many of the above-mentioned requirements).

On the other hand, the presence of an EO does not necessarily mean he or she is the highest authority responsible for business ethics, but a functional support. An example may help to understand better what we mean. When a firm bets on quality, it usually creates the figure of a quality manager who can prepare a manual on quality and procedures and even help to achieve the ISO 9000 certification. However, it is impossible for the organization to follow the path towards total quality without the senior management’s commitment to that objective, a

commitment that will exert an influence on the rest of the staff. The role of our EO would then resemble that of the quality manager in the sense that it becomes a condition that, though necessary, is clearly insufficient.

After having outlined the distinctive features of EOs, we are now going to specify the tasks they have to perform within the organization focusing particularly on the 'broad' role they must play through the strengthening of an ethical culture, and not merely on technical ethical management issues.

In conclusion, EOs should ultimately make sure that the overall ethics program reflects the organization's strategic plan and cultural values (52).

Ethical Corporate Governance. Guidelines for an ethical culture

The achievement of a set of ethical values widely shared by all the organization members must inevitably be based on the senior management's commitment to those values. In parallel, this must be accompanied by the existence of a formal corporate ethics program (although that program alone cannot consolidate an ethical culture).

Such a program should incorporate certain elements which could be summarized as follows:

1. Formal drawing up of a code of ethics that must articulate the firm's ethical expectations.
2. Creation of ethical committees, whose task will consist in developing ethical policies, assessing employees' actions and investigating ethical violations.
3. Maintenance of ethics communications systems that allow employees to report abuses and receive some action or behavior guidelines.
4. Appointment of an EO as the person in charge of coordinating ethics-related policies.
5. Development of ethical training within the firm, helping employees to recognize and respond to ethical issues.
6. Regulation of a disciplinary process that can correct unethical behaviors (53, 54, 55).

Since the decision to modify or improve ethical values is initially made at the corporate governance level, this should be the first group in the organization to assume it. This is so relevant that if these conceptions are not introduced among those who make critical decisions within the firm, they will later hardly be reflected in those decisions. So far, we could speak about the existence of a *corporate governance ethical culture*. *Culture*, because it is a set of values shared and assumed by a specific group; *ethical*, because the beliefs have that nature; and

corporate governance, because it refers to those who exercise power and responsibility for ethical entities. We cannot forget that if we want the ethical culture to make sense, it must include full assimilation by all firm members.

Under this point of view, an effective communication is essential for the ethical message to be properly assimilated (56). Only when ethical principles are effectively communicated in such a way that employees find them useful and reasonable, will employees start to accept them and incorporate them into the ethical culture. Due to the characteristics that are demanded, we think that this function of communicating ethical values can surely be entrusted to an EO. Technically speaking, information must be provided to all stakeholders about the fundamental premises of business ethics for the organization. We cannot expect all of them to subsume it. In our view, therefore, true ethical behavior is achieved through the symbolic management of ethical culture by the whole senior management.

This aspect is so relevant that through the strength of communication and the future consolidation of an ethical culture, organizations can greatly improve ethical decision-making in the workplace, not only by establishing and enforcing codes of ethics, but, also by encouraging employees to apply their personal moral standards to ethical business situations, whenever the organization's code of ethics seems wanting (57).

The mere enumeration of the values sought does not usually suffice. For this reason, support will have to be given to the modification or introduction of ethical beliefs with an approach to the symbols that makes it possible to identify the right ethical behavior. Considering the nature of ethics, these symbols will be basically intangible. Under these arguments, we can conclude that the main symbol will be provided by managers who show total congruence with ethical values in their daily activity with employees, clients, suppliers and shareholders, since once employees have been told by managers about the priorities in this field, they normally would act accordingly. These notions can be reinforced saying that ethical behavior within organizations depends on the ethical quality of their leadership (58).

In our view, whether or not it is advisable to adopt reward or punishment measures is not the most relevant thing when talking about ethical corporate governance. What really matters is symbolic leadership, insofar as all managers (and mainly the CEO and his or her close collaborators) follow these programs so that the emulation effect can pervade the whole firm.

As for the process through which ethical values become firmly consolidated within an organization, the following sequence seems reasonable: 1. organizational founders choose other

early leaders in part based on the congruence of these other people with the values of the founder; 2. these early leaders enact policies and practices that are congruent with their own deeply held values, and hire other employees who they believe will “fit” with those values; and 3. organizational members come to understand and act on the expectations of the organization regarding ethical behavior (59).

Logical as this sequence might be, CEOs must remember, however, that all members of the organization influence its culture. In other words, leaders, members and culture are systemic phenomena. A change in one of these variables will influence each of the others (60).

In short, whatever you say about your own integrity, people expect you to show it. We can only be certain that someone is honest if we observe how he or she behaves. Agreements that are not followed, false promises, deceptions, and cover-ups are all examples of indicators that a leader is not honest (61).

The EO’s role lies in the technical application of the program, as it must be taken for granted that he or she follows it. The symbolic value of corporate governance leadership in the field we are dealing with has been discussed by the literature (62, 63, 64, 65, 66, 67, 68, 69). In fact, managers who are strongly committed to ethics can influence the formal development of the ethics program. It is not only a question of formulating ethical principles; we must follow them (67). In this way, ethical failure occurs when leaders pay no heed to the fact that their behavior is well within the scope of a requirement (70). More explicitly, in terms of business culture, senior managers’ declarations about ethics have very little importance; what really matters is their actual behaviour (71). Thus, in relation to the activity they must perform, business CEOs have a significant role to play in implementing an ethical culture (72).

The corporate governance challenge is to ensure a high degree of congruence between an organization’s guiding beliefs and members’ daily beliefs, i.e. changing rules and feelings about everyday behavior. Furthermore, managers should be able to persuade an organization to change and adopt the new ethical culture.

But not only that, we must equally remember that it is not possible to bring about substantial changes in the culture of a firm in the absence of the ethical dimension of high level managers (73).

Conclusions

An ethical culture exists when a set of ethical values is shared by firm members and is not only in the mind of some manager responsible for organizational ‘ethical issues’. This can help us to understand what we call corporate governance ethical behavior. The first aspect to consider is who can carry it out. In our opinion, it is a function of the corporate governance board in general and of the CEO in particular, since the system of symbols transmitted through their ethical conduct will be a reference point for the other organizational members.

We argue that EOs cannot be leaders in ethics-related firm issues just as a result of a mere appointment, no matter how competent these EOs might be. Nevertheless, the fact that this figure exists is symbolic and meaningful, even though that is not enough. The delegation of ethical management by the firm’s corporate governance cannot have a strong cultural effect, as it is the senior management that must be responsible for ethical issues. Designing formal ethical programs that can later be specifically formulated and implemented by the EO is undoubtedly useful. The aim we seek is to strengthen an ethical culture, and not only the technical aspects of ethical management.

In the end, senior managers will be required to show their interest in these programs through their commitment to them, since the success of those programs will depend on their symbolic management. We are thus firmly convinced that *corporate governance ethical culture must necessarily include the conversion of the CEO and all the senior managers into symbolic EOs, which will reinforce and give sense to the formal appointment of an EO.*

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