The Morality of Doing Business Purposefully

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Corporate scandals are often seen as a lapse in corporate governance mechanisms. However, it could be that corporate governance codes and measures are too focused on utilitarianism, and insufficiently on the moral foundations espoused by deontology and virtue ethics, which would shift a company from an absolute emphasis on profit maximisation to its purpose or mission.

In recent years, corporate scandals and news of wrongdoing in government, for-profit and not-for-profit bodies have captured our attention. Whether it is Volkswagen cheating on emission results, Samsung allegedly guilty of bribery and embezzlement, or Oxfam's senior executives accused of sexual impropriety, the headlines make a gripping read.

In the Wells Fargo scandal, where the US bank created millions of fraudulent savings and checking accounts without the consent of its clients, a headline in *CNN Money* (April 2017) demanded: "Where was the board?"

Even in squeaky-clean Singapore – which has consistently ranked among the top 10 least corrupt countries in Transparency International's Global Corruption Perceptions Index since it was first established in 1995 – there have been headline-grabbing lapses in corporate governance.

While it may be possible that board members – individually or collectively – were unaware of the misbehaviour of company executives until the scandal hits the news, this cannot be the basis for the board to abrogate its responsibilities.

Code of conduct and ethics

Corporate governance broadly refers to the system of rules, processes and practices that helps a company make effective decisions in its long-term interests.

The recently revised Code of Corporate Governance in Singapore takes as its starting point a recognition that the board has the dual role of setting both the company's strategic direction, and its approach to governance. It emphasises that this includes establishing an appropriate culture, values and ethical standards of conduct at all levels of the company.

The board and management, who make important decisions but are not the major owners of the company, should not be tempted to indulge their own preferences. Rather, they must act as responsible agents of the shareholders.

For that reason, corporations across the globe are increasingly making significant changes to their corporate governance policies. Specifically, they have started increasing the presence of independent directors, emphasising demographic diversity, and allocating board leadership to an independent Chairman. These, and other measures, ensure a more effective board.

Based on our research, we highlight in the table below the six common criteria used in codes of corporate governance to promote board effectiveness.

The Six Common Criteria in Codes of Corporate Governance

INCLUSIVITY

- Treating all shareholders equally and fairly
- Enabling all shareholders to exercise their rights
- Engaging all shareholders and promoting effective, balanced communication

ALIGNING INCENTIVES

- Having a transparent procedure for remunerating individual directors and key management personnel
- Ensuring that the level and structure of remuneration are aligned with the long-term interests of the firm

MEMBERSHIP

- Having a transparent process for appointments and reappointments
- Regularly reviewing the needs of the organisation and changing the board structure accordingly

SELF-MONITORING

- Regularly assessing the effectiveness of the board and the board committees
- Regularly evaluating the contributions of each director on the board

CONDUCT & COMPOSITION

- Having an appropriate balance of independence
- Having clear division of responsibilities between the board and the management
- Promoting diversity of skills, knowledge and experience

MONITORING THE ORGANISATION

- Determining the level and nature of risk a company is willing to take
- Ensuring that the management maintains a sound system of risk management

Three foundations of morality

There is some scientific evidence, primarily from data collected in the US, to suggest that some of these changes will potentially reduce breaches in corporate governance practice.

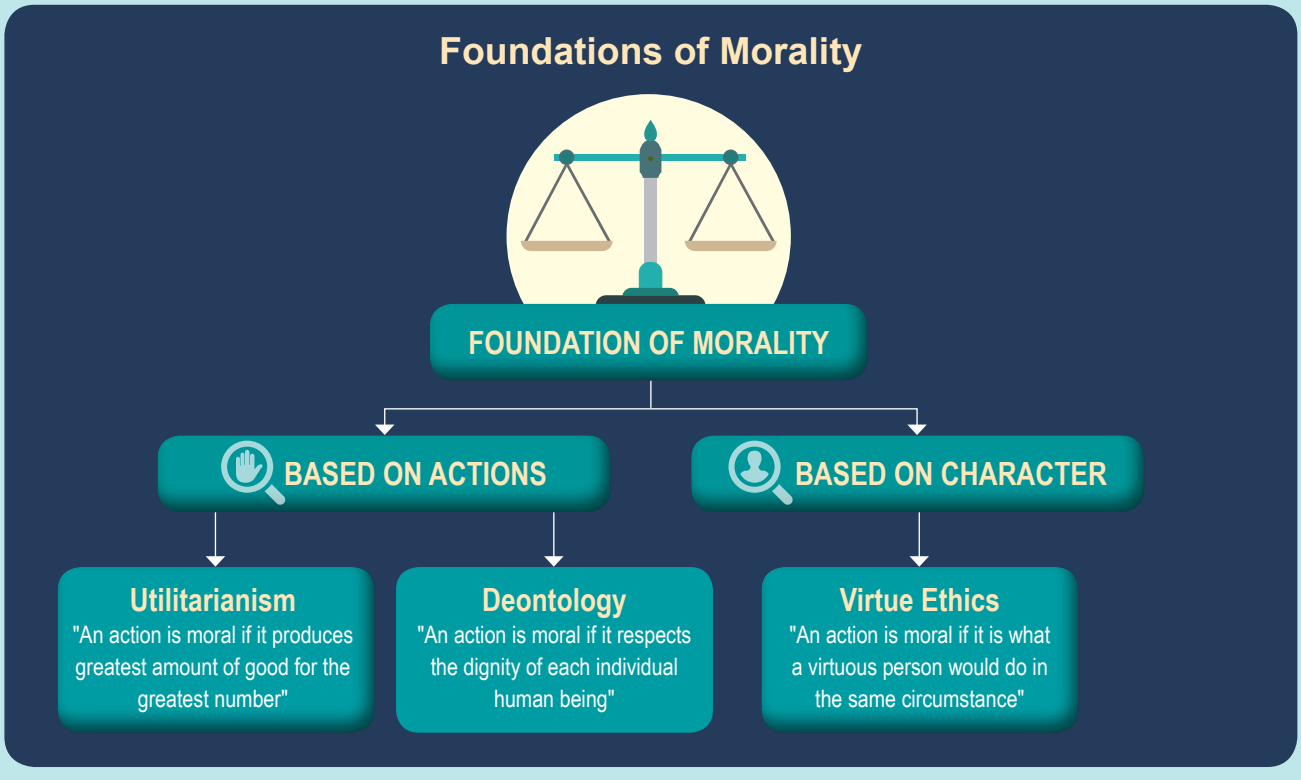
However, this picture is incomplete because the guidelines tend to be based solely on the utilitarian foundation of morality, while ignoring the other two foundations of deontology and virtue ethics (see diagram below).

The three foundations of morality stem from different worldviews, and consequently take different approaches to setting out the ethical standards that guide us.

Deontological ethics, or deontology, is sometimes described as ethical standards based on rules, duties or obligations. It tells us that there are some rules that we ought to follow and duties we ought to fulfil even if these prevent good outcomes from happening or may even result in bad outcomes. The fundamental duty of individuals and corporates is the categorical imperative, which is to respect the dignity of each individual human being. Simply put, we should treat others as we would want to be treated and every human being has a right to be treated with dignity and respect.

Virtue ethics are based on character traits, such as having integrity, being honest and truthful, being tolerant, and so on. In essence, these are qualities that constitute a good and meaningful human life. Such a foundation of morality shifts the focus from what the person should do to who the person is. It encourages companies to develop cultures and design systems in which people can act virtuously.

The third foundation of morality, utilitarianism or pragmatic ethics, directs us to decide how to act, based on the overall consequences of our actions.



Primarily a consequence-based theory put forth by theorists Jeremy Bentham and John Stuart Mill, this approach proposes that maximising the overall good brings about "the greatest amount of good for the greatest number".

According to utilitarianism, the ultimate ethical goal is to produce the best consequence for all parties affected by a decision and thus, any decision that does not accomplish this goal is ethically wrong. The idea of "profit maximisation" is based on this world view and corporate governance systems are primarily intended to fulfil this organisational mission.

Designing corporate governance policies based on utilitarianism alone raises a moral challenge. Since its essence emphasises outcomes, and ethical and unethical acts are inferred from their consequences, it follows that the ends justify the means. In reality, we know that this is not always the case. Profit maximisation cannot be the only goal. For example, a firm would probably increase its profits by lowering its labour costs if it used children to make cheap products. Such practices, however, violate the basic human rights of children.

When the principle of utilitarianism does not necessarily promote behaviours that are in line with ethical standards and societal norms, it may lead us to question whether an exceptional focus on utilitarianism in our codes of corporate governance and a "compliance" mindset is actually the most appropriate model. In other words, sometimes, the utilitarian way of directing and managing the firm should be addressed by incorporating deontology and virtue ethics into the company's corporate governance policies.

Organisations with purpose

Clearly, corporate scandals and misconduct are orchestrated by a few, but affect many. It is important to recognise that there are some outstanding models of good governance, and to reward such good behaviour because, more often than not, these organisations have a corporate culture that is based on "purpose".

One way of doing so is to shift from an absolute emphasis on profit maximisation to one that integrates the purpose, or the mission, of the company.

With this perspective, the focus moves beyond asking questions about whether the company is maximising profits or which actions are legal and, instead, engages in a search for its true sense of purpose.

This search involves asking questions such as: Why did this particular business begin? What did the founders want to achieve when they started it? How does the business understand itself in relation to its stakeholders, to the industry, and to society? And what is it doing to create a shared sense of purpose?

A focus on purpose underscores the interdependence of business and society, that business success is intertwined with the success of society, which in turn allows the business to flourish. Thus, one cannot thrive without the other.

We know, from several decades of research, that employees are affected by their work environments, and good behaviours can be encouraged and characters nurtured. Therefore, the way in which business leaders describe the purpose of the business, and the dedication and loyalty they inspire in their employees, can have a great effect on how their employees feel about their responsibility for one another and the wider community. The table on the next page lists six values that could potentially help companies find and achieve their purpose.

Achieving Purpose: Six Helpful Values

DIGNITY

Businesses have a responsibility to view each employee as a someone, not a something and to treat employees with respect and dignity and to promote their fulfilment.

SOLIDARITY

Business actions operate in the context of the values, expectations, and needs of communities, particularly, by looking for ways to help the underprivileged, underserved and the disenfranchised.

PLURALITY

Businesses can accomplish their purpose by creating a context that minimises constraints and creates opportunities for diversity.

SUBSIDIARITY

Businesses should promote accountability at all levels by proper delegation of decision-making.

RECIPROCITY

Businesses should provide opportunities for mutual benefit in that employees receive what they are entitled to and can reasonably expect from the organisation.

SUSTAINABILITY

Businesses should seek to replace what earth's resources we use and repair what we damage and strive to leave the planet in a better condition than that in which we found it.

Source: Hollensbe, E., Wookey C., Hickey, L., George, G., and Cardinal Nichols V. 2014. Organisations with purpose. Academy of Management Journal, 57(5): 1227-1234

Integrating profits and purpose

To avoid ethical failures and compromised moral behaviours, companies can take steps to integrate profits and purpose into governance practices. But how should the board ensure that the company's objectives are fulfilled while safeguarding shareholder value?

First, the company should design a comprehensive performance management process that supports the purpose of the business. We know that people perform better when their actions are measured and rewarded. Therefore, the board needs to focus on delivering results while accomplishing the business' purpose. That is, it needs to marry the "what" with the "how".

The board can also engage in an exercise to reflect on its true purpose and how the six values of dignity, solidarity, plurality, subsidiarity, reciprocity and sustainability can be imbibed to achieve this objective. These values can then be translated into behavioural metrics for which management is held accountable. The alignment of the goals and rewards with the company's true purpose is likely to work as a governance mechanism which considers all three moral foundations.

Extensive academic research has found that having a strong disciplinary system in a company is better than having no such system, but having a weak disciplinary system may be worse than having none. It is thus important to ensure that violators of the purpose of the company are punished in a way that is commensurate with the transgression, thereby sending a signal to all members of the company that the board truly endorses the purpose.

Next, the board should appoint a "purpose committee". There is evidence that when people are contemplating whether to report (whistleblow) problems at work, they conduct a decision calculus based on two factors:

- Efficacy: the person's perception about whether speaking up will be effective in bringing about the desired result, and
- Safety or risk: the person's perception of whether reporting problems will have negative consequences for himself or for his relationships with others.

The core idea is that people are more likely to speak up and report problems if their judgements of efficacy and safety are high. In fact, beliefs about efficacy and safety are the driving force behind whistleblowing behaviours, and these factors outweigh other elements such as ethical leadership, presence of ethics, and compliance programmes.

To ensure that employees are encouraged to speak up, it is essential to create a "purpose committee" of the board. This committee of non-executive directors should be responsible for creating a robust programme of controls and processes to promote conduct in line with the purpose of the company.

The committee should be charged with working with senior management and other board members to ensure that the company's purpose forms an integral part of its overall business strategy. It should be the main point of contact for all employees who want to anonymously and confidentially raise any problems related to non-compliance of organisational members, including the top management, with the purpose of the company. Such a committee would signal high levels of efficacy and safety to the employees, thereby encouraging them to speak up.

Finally, the board should mandate interactive training programmes, especially for newcomers. These can help companies achieve their purpose. There is plenty of scientific evidence which suggests that when that purpose includes dignity by encouraging employees to express their personal identities at work, they develop pride in their company and internalise its values.

Training can also help companies achieve purpose through solidarity. For example, women are historically under-represented in the formal labour force. Research suggests that women in developing countries face psychological and social barriers that force them to drop out soon after joining. Workplace training conducted by experienced trainers can reduce dropout rates by inculcating work-readiness learning, such as self-reliance, interpersonal communication, self-presentation, and work-life separation.

In summary, the ethics of good corporate governance should motivate boards to move away from focusing on profit maximisation as the company's sole objective and to incorporate purpose into the equation. In particular, boards need to reflect on their governance processes and question whether their internal structures for decision-making and rewards are solely utilitarian or if they should integrate deontological and virtue-based ethics.

In the long run, our view is that good ethics makes for good governance. ■

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