

Preemptive Action in Changing Times

How Management Can Ensure the Highest Probability of Ethical Behavior

Let's face it. In the era of the corporate scandal, leading a major corporation -- in a senior management role or as a board member -- has become a very difficult and time-consuming job. As investigations continue and the question persists, "Where was the board?" tensions have risen across the boardroom table. Board members and senior management alike are expected to uphold increasingly higher standards. In some cases, WorldCom for example, they are being held personally responsible for corruption and mismanagement within the ranks of their corporations. All of which begs the question: what can be done to meet that new standard? Here is my advice to senior management, a few well-crafted tips to take preemptive action and ensure the highest probability of ethical behavior.

Firstly, start at the top. Get used to a new and integrated arrangement with your corporate board that holds all parties accountable. It used to be very common to have a chairman and a CEO to have that link between management and the board. Now it is much more likely that the board will have a non-executive chairman or a lead director. We in the US have often emphasized this sort of board independence. We've looked for outside directors who have no conflict of interest with their own careers that might link their success and personal fortunes directly to the company's performance or the company's activities. Comparatively, the model in Europe and Japan is very different; managing directors have risen up through the company and end up on a management board. The boards in these models really are integrated with management. They have intimate knowledge of the company's practices and procedures, honed over long periods of time working within the ranks of the company. This is the direction we need to go in...and fast.

In order to meet the task at hand, senior management needs to establish more than one channel of communication between the board and the daily operators of the corporation. A good board will be getting information from multiple sources. Obviously, the CEO and senior management will be one channel. Independent audit functions will be another channel. Perhaps they are receiving information directly from contact with governmental regulators. But is there an ethics function within the company? Have you set up an ombudsman in the company? Are there people that the board can turn to whose job and performance is measured by their ability to identify broad issues within the company, cultural issues, or significant and risky gaps in training?

Secondly, establish effective two-way communication mechanisms for all employees. One of the questions we had when Boeing was putting together their ethics program was, "Where was the vertical channel of communication?" There was going to be an ethics panel that was going to coordinate all the ethics functions throughout this massive enterprise. But where was it going to get reported up to the GC? Where was this going to be reported up to the board? How do things get reported up? It should be happening.

If you are a Boeing, an Enron, a P&G, or any massive institution, you have hundreds of thousands of employees operating in a web of transactions that could have national security/economic implications. For a smaller company, the risks might be smaller, but equally significant to the success of the company. Do the people who are performing the day-to-day tasks have a mechanism to interact with you and your board? Is there somebody that an employee can report to, even at a relatively low level? Be sure that there is an ethics official to whom an employee can say, "I have a problem here. I don't think this is being handled properly. I think my boss is pricing this incorrectly, or somebody is stealing from the company." At some companies, it might be a telephone hotline or an ombudsman. Perhaps you create a more informal structure. Maybe you have a sit-down in the coffee room every three months or so with some lower-level employees -- people from the GC's office, significant manufacturing people, accounting people -- and ask them, "What's going on? Are there any issues? Please know you can come to us."

Next, identify the greatest risks and be proactive about managing them. Judge Cardozo, when he was on the NY Court of Appeals, once said, "The risk that is perceived defines the duty to be obeyed." You should maintain your senior management role within a corporation (i.e. don't allow the board to take on your duties), but you can be aggressive about identifying the risks that exist that may prevent you and the board from serving your financial and ethical duties. For some companies, there might be accounting risks, as we have seen in so many of these cases, or transactional risks. In other companies, it might be product liability. Still in other companies, it might be labor or cost of materials. Identify the most serious risks and focus at least some attention on how those risks are being handled. Maybe that's a moving target, but it is worth hunting down and giving some level of energy to minimizing.

Lastly, establish positions within your corporation that are responsible for dealing with the company's regulators or dealing with government officials and important constituencies. With a company like Boeing, it's going to be their principal customer on the defense side, the DOD. On the commercial side, it is the FAA. With a bank, it will be the Comptroller of the Currency or the Fed. Make it their business to say, "We would like a periodic meeting. If you have a problem, come to us when it is a little problem before it becomes a big problem." In that way, there becomes a two-way dialogue. If you are a toy company, designate somebody, a senior management committee, who can sit down with the Consumer Product Safety Commission and say, "If you have an issue that you would like to bring to our attention, we would be happy to talk about it. We would like an hour of your time once a year or once every six months just to talk about how we are doing." Things will happen. An individual employee, for venality or lack of intelligence, can get a company in a lot of trouble. But if something problematic happens and you have a relationship with a regulator, they will handle the problem differently.

Senior management is not the ultimate guarantor of ethical behavior within a company, but you need to consider whether or not you are taking the right steps, the extra steps, and whether or not you are asking the right people about events and developments within the

company. You have a significant duty to meet, one that increases as the risks of your operations increase. And as the national and world business communities and governments hold you – and your boards -- more and more responsible, it is prudent that you do your part to ensure ethical behavior at every level of your company.