# Implementing Ethics in Business Organizations★

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ABSTRACT. In view of the scope and scale of the latest scandals, e.g. Enron's maximum breaking bankruptcy, the re-discovery of ethics in business has received an impressive boost. By now even car salesmen have written ethics, "a Code of Conduct", e.g. in the USA or Poland. But there is no clear aim of the role ethics obtains in organizational settings as we may show in some small cases of practical approaches to deal with ethics in organizations. We discuss how ethics is the prerequisite to conduct any business and what advantages may be realized if a clear set of ethics is followed. We will discuss three practical examples. In cases of ethics-based values-added management of Siemens (Germany), Boeing (U.S.) and SAP (Germany) we explain the mechanisms of ethics in management to strengthen organizational success. We emphasize the importance of clear ethics-related communication processes in organizations. We explain the use of communication theories inside organizational processes to clarify communication about such an abstract topic as ethics. Finally, we point out how a management of ethical ideas and cultural values should be designed in business enterprises.

KEY WORDS: business economy, communication system theory, corporate ethics, definitions of "good", Institutions, values-based management

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## Ethics as a prerequisite to conduct business

*Ethics: pure necessity*

Ethics, in the sense of an accepted set of rules are a prerequisite to any transactions. Parts of the rules are – or may be – covered by legal stipulations. However, these can hardly ever be fully comprehensive or up to date. Plus: laws and regulations are usually the reflection and outcome of a clear and sanctionable set of morals that is understood as commonly given by the society that institutes and follows them.

A liberal, capitalistic-oriented economy can function only if the participants and the responsible players follow a certain set of ethics. This "value canon" means, for example, that bills are to be paid, contracts are to be kept, employees, shareholders, competitors, suppliers and customers are treated according to existing contracts and the law. Only if a large majority of players in an economy adhere to these principles can this economy function properly. These principles thus constitute the foundation of the economy.

According to Schumpeter, the commercial and industrial society has been cast in an economic mold: its foundations, beams and beacons are all made of economic material. Prizes and penalties are measured and communicated in pecuniary terms. Within this frame this social arrangement is – or in any case was – singularly effective (Schumpeter, 1976, p. 73). It created a schema of motives that is unsurpassed in simplicity and force. The promise of wealth is strong enough to attract a large majority of people in a society and success comes to be identified as business success (Schumpeter, 1976).

Schumpeter goes on to say that if, however, there were a way of measuring either this ability in general or the personal achievement that goes into any particular success, the premiums actually paid out would not be found to be proportional to either.

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Spectacular prizes, much greater than these would have been necessary to call forth the particular effort are thrown to a small minority of winners, thus propelling much more efficaciously than a more equal and more "just" distribution would, the activity of that large majority of businessmen who receive in return a very modest compensation or nothing or less than nothing, and yet do their utmost because they have the big prizes before their eyes and overrate their chances of doing equally well.

In recent years we have seen a dramatic increase in the willingness of managers to submit to unethical or illegal – or both – behavior in order to belong to the small minority of overly compensated "winners", in the sense of financial payments. In this respect we can say that the value or measurement system of capitalism has already outlived itself, since pecuniary advantages can be achieved not only by efforts and efficiency but also by bending the rules according to one's need in order to beat other competitors in the markets.

Taking this development into consideration we are already on the road described by Schumpeter, that is that capitalism by its success will reinforce rationalism and will give it a bent in certain directions – rationality comes to mean thinking for yourself, seeking individual self-interest. This seems to be happening already. The next step would then be that the spread of rationality in such a sense undermines traditional values and institutions, and eventually undermines bourgeois values and institutions, i.e. undermines the legitimacy of capitalism itself. This is where the relevance of business ethics seems to be – or may even need to establish itself. If a society is watching itself and detects the phenomena of its values and institutions being undermined, how can it react to make sure this basis for its system of social organization can survive? Thus, we have a role for business ethics on a macro-economic level. In this sense its role would be to show what dangers the loss of traditional values may bring, that is, according to Schumpeter the destruction of capitalism. Its role would also be to develop theoretical approaches and practically applicable means of how to avoid, stop or slow this process. That is how to show the relevant players in the current social system that ethics is, indeed, a pure and inherent necessity. Apart from this, the role of business ethics would also be to show the advantages of ethical behavior in the existing social system, which is the next point in this article. This would bring ethics from this macro-economic perspective to the level of micro economics, i.e. of organizations and institutions.

The interrelationship between these two principles – the establishment of self interest as rational principle and at the same time the unobtrusive function of traditional values – will be the challenge of business ethicists. Mandeville named in his "Fable of the bees" the benefits of pure self-interest for the social life: "The worst of all the multitude did something for the common good" (Mandeville, 1714, p. 24, Part G). But at the same time he showed the problems of the absence of self-interest as rational principle of a society under the control of virtue and ethics: "Fraud, luxury and pride must live; whilst we the benefits receive" (Mandeville, 1714, p. 36, Part Y). At the end Mandeville pleads for the care for a social network of self-interest and virtuous care for traditional values and institutions at the same time. He named the dangers of pure self-interest and the need of strict social functions: "So vice is beneficial found, when it's by justice lopt, and bound" (Mandeville, 1714, p. 37, Part Y).

In particular it must be demonstrated that ethical behavior will prove to be advantageous. A reinterpretation of the widely taught Adam Smith has led a majority of businessmen and executives not to think so. Smith "invented" the "law" of the market. Thanks to the "invisible hand" of the market, he believed that self-interest which drives men "private … passions …" are led into the direction "which is most acceptable to the interest of the whole society". Thus competition will regulate "self-interested profiteers". But Smith also considered the need of the basic structure that links the self-interest efforts as "invisible hand".

Generations of students have been schooled to believe that man is essentially an acquisitive creature, the profit motive being as old as man himself. But it is not. It is only as old as "modern man" (Heilbronner, 1975). There is, in fact, no evidence, that self-interest maximization provides the best approximation to actual human behavior (Letiche in: Sen, 1992). For all the new 20th century developments, society still believes in the "*laws* of the markets". What Smith meant was one thing, what proponents make him out to mean is another. He was made into the "guru" (Sen, 1992) of self-interest as capitalist protagonists have known very well how to interpret Smith's work to mean ''leave the market alone'' and, more importantly in this context, ''self-interest is good'' but: only if you know the substantial contents of the invisible hand.

*Advantages of ethical behavior*

From a neo-institutional economics point of view two theories will be used here to explain the advantages of ethical behavior. Both theories combine the advantages of a self-interest based heuristic with the power of social constraints.

The transaction cost theory judges the efficiency of business transactions by production and transaction costs (Williamson, 1979, p. 22). Ex-ante transaction-costs are e.g. information-, negotiation-, and contract-costs. Ex-post transaction costs are e.g. costs of controlling and risk minimization. Business partners that adhere to a clear set of ethics are able to minimize (e.g. negotiation, information) or even abolish (e.g. controlling, risk minimization) some of the costs. An example is the ''handshake'': when both business partners know this to be a binding finalization of an agreement. There are no contracts (and therefore no fees or expenditures) to draft, set up and sign and no costs arise to then monitor their fulfillment. The more certain the business or transaction partners can be of each others values and behavior, the lower are the transaction costs.

The focus of the principal-agent theory (Alchian and Demsetz, 1972) is on the questions of advantages and disadvantages that arise in transactions between the principal (owner or ordering party) and the agent (contractor). Information is asymmetrically distributed and – see the usual interpretation of Smith – as both the principal and agent will always try to maximize their individual self-interest, the problem will arise that the agent may or will use his better information to the disadvantage of the principal. There are four types of agency relationships: hidden characteristics, hidden intention, hidden action – which will lead to *moral hazard* (Trumpp, 1995) – and hidden information which can also lead to *moral hazard*. The risk of an agency problem or moral hazard is all the higher, the uncertainty about the motives, the bigger the alternatives and preferences of the agent. The more both principal and agent believe in the same values and adhere to the same fundamental ethical convictions, the smaller the uncertainty and the moral hazard will be. Ethical behavior in the sense that both, the agent as well as the principle, want to create a win-win situation for both partners would mean here that the problem of a conflict of two different individual maximizers of self-interest would not even be there to start with. A moral hazard would not exist were it not for the assumption of ''individual maximization of self-interest''. Were it not for the creation of the ''Homo Oeconomicus'' this problem would not exist to be discussed.

*The difficulties with ''good''*

The difficulties with ''good'' start with its definition – or the near impossibility to define it. From a historical point of view, different understandings of ''good'' are offered. Plato believed that in the end we could at best find the ''idea of the good'', Aristotle thought the good to be the ''collective well-being''. The Christian view thought that to be good was to aspire to be as similar in actions and motives as Christ, respectively God. Ethical inquiries start with the question of what is good. Moore showed the difficulties of defining what is good.

Companies cannot rely on ''higher authorities'' to follow on what they take to be good. In order to make sure that the members of an organization or company understand and – at least partly – share those values a company intends to stand for, a company needs to work on the development and definition of these values. There are different approaches to developing values: top down and bottom up approaches to develop a set of values. In the following we discuss the examples of Siemens, Boeing and SAP.

## Discover and develop values: the need of a clear set of ethics

Values are an intrinsic part of cultural behavior. The characteristic of this role of values needs a sensitive style of communication in organizations. In the following examples we explain three ways of dealing with the challenges of communication. Each example shows unique facts of organizational communication empowering or dismissing personal engagement with ethical values.

*Boeing: Strictly protective compliance- and values-management-system*

The Boeing Corp. has established a traditional way of dealing with values based issues in organizational ethics. Boeing defined the kinds of behavior that they considered dangerous and harmful to the company. Priority is related to legal issues (U.S. law) and regulative requirements (Security Exchange Commission, Department of Defense, Defense Industry Initiative) as a quoted stock corporation, which makes a large part of its turnover and profit from public orders in the defense area. Boeings work is traditionally closely intertwined with public-sector administrative bodies. Boeing had to be careful to avert penalties and exclusion from public orders on the grounds of unfair trading. Day to day work and decisions are related to public decisions and many managers came from a background of public administration before joining Boeing. Because of close relations and high dependence on public orders they had to establish corporate values, fixed basic rules and a training program.

The Boeing ethics program is a response to the federal government program against waste, fraud and abuse. They established a management guideline (''business conduct guideline'') connected to an ethical management controlling system and a commitment to strict consequences for misbehavior. In relation to these themes Boeing built up a protective value-management system comprising:

1. Ethical business conducts,
2. Proper marketing practices,
3. Offering business courtesies,
4. Acceptance of business courtesies,
5. Conflicts of interest,
6. Proper relationship with suppliers,
7. Dealing with former U.S. government employees.

*Siemens: Intrinsic cultural values as leadership competence*

What prompted Siemens to establish values-management was the need to integrate cultural and individual peculiarities into corporate communication processes? More than optimizing the fundamental corporate structure, the value-management process at Siemens is driven to optimize soft-facts of communication (Figure 1). Siemens took calculated measures to avoid complications with ethical behavior in the international context and to integrate people with different ideas into the ''Siemens Family''. As a side effect, value management should improve the success of the company's businesses. Management of intrinsic values of the managerial and organizational approach requires highly developed informal structures.

These informal structures are part of the Siemens tradition:

1. Focus on financial results with strict financial control,
2. Strategic and technical management without consideration of values,
3. Realization of strategic orders without support of ethical values,
4. Clear managerial focus on technical and economical contexts,
5. Focus on individual personal development,
6. Top-management is recruited from complete Siemens careers.

The term ''Siemens Family'' stands for written rules and a fixed set of social values that due to their complexity could not be captured by basic rules or guidelines. The complexity and vagueness of the ''Family'' value-idea often lead to problems for new managers who join the company.

*SAP: Facultative ethical values*

SAP has established no explicit corporate values. They care for social communication about values for

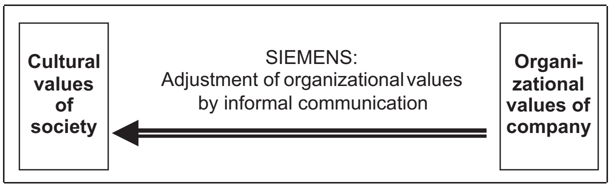


Figure 1. Value adjustment as organizational function at Siemens.

a very different reason: SAP has a very ambiguous style of teamwork, where the teams are set up independently from hierarchical restrictions. SAP supports its basic organizational structure by offering and encouraging team values, in which managers and employees often change team members in a self-organizing way. The cooperation of the teams is mainly oriented on customer projects. Employees have to feel good in the teams, if they do not they are free to leave the teams. SAP therefore has no binding set of core values structuring individual behavior but offers key rules for cooperation. Often team leaders fail to communicate their individual core values in sufficient ways.

These key rules are:

- Quality: Solving quality-related problems.
- Development process: Optimize the use of information technology throughout your enterprise.
- Cooperation and communication: Working together constructively to find the best possible solution.
- One big team: We do not think much of hierarchical structures and bureaucratic procedures.
- Long-term partnership.

Beyond these rules all managers and employees have to find their own rules of cooperation. This values-based effect is stressed by the fact, that all managers have no fixed number of employees, but have to win team members for each project they run. Corresponding to this, employees are able to select those projects and those managers with the most fitting values. This way SAP creates an internal job market that guarantees the changing of and adapting to values in organizational structures. A communication process evolves that structures values-based topics in a self-organizing way. But often the values communication process is lacking and the team members are unsatisfied and only relate to short-term tasks.

## Communication of abstract issues such as values in organizations

### *Value communication in organizational processes*

The three examples of corporate practice with ethical issues show three types of communicating values in organizations: (a) Directive fixing and supervising of concrete means (Boeing); (b) providing a basis of communication for the adjustment of corporate values and cultural principles (Siemens); (c) creating a self-organizing environment for the communication of individual values to set up successful teams (SAP). The main differences of handling values can be seen in the way values are communicated: as a fixed part of their structure or as a medium for ethical communication to create an organizational framework.

These two aspects of ethical communications are related to the ideas of consensus and impulses: The creation of consensus in various repeating discourse processes to meet reasonable approval and the communication of impulses as a framework of communication with the goal of commitment of all participants. The main challenge for both types is to judge the rationality of organizational goal-orientation and within this context the ethical dimension of communication processes (Table I).

"Consensus" means the correspondence of thinking of several individuals: two or more individuals come to a shared meaning (implicit and explicit) of thinking in several steps communication. This leads to three questions: How is the consensus-oriented

TABLE I

Two approaches of value-communication: discourse and commitment

| Discursive creation of moral consensus | Communication of expected value-commitment |
|---|---|
| • Communication without influence of power<br>• Everybody is enabled to pronounce his ideas<br>• Shared meaning of accepted values | • Position of leadership is visible<br>• Expected values are goal oriented<br>• Values are related to targets of the organization |
| → Correspondence of thinking | → People demonstrate their commitment |

communication process designed? Is it possible to link means of individuals so closely, that an "identity of ideas" can emerge? Is there a basic difference in individual interpretations of ideas, so that we will have to speak about consensus in gradual steps?

These questions can be discussed from a Habermas perspective. He transferred the question of normativity from a content-oriented position to formal aspects of normativity (in consequence of the impossibility of metaphysician or ontological value patterns). Habermas transformed normative aspects of values into formal design of the communication process. He postulated the normative character of the ethical discourse requiring a process of frankness and many repetitions (Habermas, 1981, 1993a). Consensus of meaning between individuals in these terms is related to frank discursive communication processes. Only the structure and practice of discourse decide about the normative validity of the results. Habermasian discourse principles are designed to create understanding of values in consensus of all participants under specific restrictions: Correspondence of thinking between two subjects; Shared view of meaning of values; Homogeneous means of consciousness; "Understandability" of individual values; Communication process without influence of power; equal chances of participation for all participants; frequent repetition of discursive processes. Again: Not the resulting consensual values are normative, but the structure of the discourse itself.

Luhmann criticized this position of a discursive creation of ethical consensus. Luhmann criticized the possibility of a linked meaning without differences. Even for organizational reasons he denied the fiction of a timely unlimited process and the illusion of frequently repeated discourses in society and organizations. However, more than this he criticized the impossibility that two subjects can get to a point of full understanding of each other. There are no objective criteria to asses whether one has the right understanding of the means of values and words of someone else. There is an impossibility of evaluating homogeneous means. Luhmann set the stage to speak about communication processes in the area of moral communication (Luhmann, 1995) and not about substantial values.

As a consequence, values, norms and rules are visible only in communication acts (sic: Parsons, 1951, 1968a; Spencer Brown, 1971; Luhmann, 1992). The act of value-communication is now the relevant act itself (more so than values as contents). In a "market of communication", ethical values and entrepreneurial ideas compete among others to create an organization. They succeed in commitments, where some ideas are superior (Luhmann, 1992; 1993). Commitment is the main criteria to evaluate communication processes.

### *Communication and commitment*

Entrepreneurial ideas in a market economy draw their opportunities and, therefore, their strength from unknown actions and reactions. Almost "not expected" events create new opportunities in new situations. New business ideas grow out of opportunities with outstanding success only in "unregulated territory". Opportunistic behavior – in other situations the reason for conflicts – is the impetus for innovations (Williamson, 1979, 1985). There is a fundamental need for the avoidance of consensus to achieve entrepreneurial character, success and innovative power. To be ahead of the average, competitors need innovative actions and events, which are not ruled by social or organizational consensus. It requires consciousness of the organizational goals and their communication to employees, investors, customers and strategic partners. These stakeholders are interested not in consensus-oriented rules but in differentiating themselves from competitors. Commitment is the pragmatic approval of concerned individuals to back up organizational ideas. Organizations depend on entrepreneurial success. They need structures for value-communication to protect the space of individual characters and even to avoid consensus in the society or market community on aspects of their organizational competitive advantage.

The agreement on market rules is a commitment of market participants to respect market rules. Beyond this rule the market economy needs inhomogeneous behavior, sensitivity and creativity. Even the rule itself has to be incoherent and open for different interpretation in order to be the origin for corporate success. Within this understanding, a market economy needs a defined "space", in which one can create ones own successful values. These then compete with others. The creation of this "space" is an ethical responsibility. The result will be a framework of behavior in the market economy which guarantees both fairness against others and freedom to do new businesses in new ways.

The ethical judgment of values and behavior changes the subject. The goal is to create a "surrounding of possibilities". This enables individuals to exercise their own responsibilities. This responsibility is relevant in decisions for values, which compete against other values and may prove to be superior. The "surrounding of possibilities" are the realm of values, the soft-law, and the rules of the game. Beyond these rules, there is space to develop ones own specifications of values. The ethical evaluation of this surrounding is to judge how it ensures the chances of individuals to compete with their values in solving problems and challenges.

### *Practical requirements for values-based communication*

Classical theories about the functions and mechanisms of giving new impetus inside organizations recommend setting financial goals to incentivise top performance. These elements initiate behavior in traditional ways and are related to conventional economic intentions. As a stage to communicate a certain orientation in understandable ways, they have to enable the organization to reach its goals. But additional mechanisms are necessary to give impetus to articulate the soft-law area of management and co-operation and to avoid frictions and conflicts. Such mechanisms include "soft facts" of moral communication for integrating moral values and structuring the area of emotions and behavior. Organizations push their values in the direction of their tasks. Value-communication is a communication to give innovative impulses. Value-communication increases orientation and transparency and improves the effectiveness of normative rules and advice. The explicit communication of moral values clarifies the meaning of advises and organizational handicaps with additional explicit impulses. As a tool of corporate governance and controlling it relates to the following aspects:

- Definition of organizational goals to determine the use of the organization
- Deriving measurements, incentives, instructions
- Making implicit aspects a subject of management
- Analysis of intrinsic goals of the stakeholders
- Pronouncing expected responsibility
- Creating a communicable "Soft-Law" of behavior.

The particular communication of visions and emotions requires mechanisms in organizations, which go beyond the classical tools of management. All members of the organization need to relate to the rules of organizational visions and ideas. Mechanisms are necessary that adjust the behavior of the participants, even if the incentives in organizational structures are not compatible with the goals that should be achieved (Wolff, 1999). Processes of value-communication must harmonize valuecommitment and a transparent soft-law: Both, hard-facts and soft advice need to be understandable. These commitment processes are adjusted against goals and objectives as well as entrepreneurial visions and emotions of an organization. Participants should be enabled to evaluate whether they want to adapt themselves to the values and goals of the organization or not.

### *Ethical commitment as a process of communication*

Ethical commitment is the acceptance of values of the company (or team) for you and your colleagues to build a social group. It is the acceptance that these values are not inevitably obligatory to other social groups but necessary for the cooperation in the group you belong to (Luhmann, 1992, 1995). Moral communication will add efficiency in organizational communication processes. It builds a core agreement on substantial basics. It complements traditional communication of goals and targets, which create frictions, as they are not clearly understandable to all participants. Committed values create an area of understanding, in which non-explicit messages get clear and understandable because of explicit soft components. The kind of moral values an organization or a society uses in its own communication processes is irrelevant to the functioning of this communication. Important for the communication process in principal is communicating the most fitting values to achieve the respective goals and to communicate with these values the implicit aspects of leadership.

On the other hand, organizations are always coined by participative structures. Participative organizations have strategic impacts from several participative groups. They take a high notion of the freedom of members to participate in autonomous decision taking and creativity (Collier and Esteban, 1999). The communication of moral values in organizations with elements of participation can structure the communication more effectively in terms of a "core line" for constructive integration and for controlling of value dilemmas (Hampden-Turner, 1994). The mixture of both hierarchical and participative aspects of organizations requires a level of communication that examines the intrinsic aspects of the organization and the individual behavior and makes them explicit. Value-commitment is a permanent process of communication in an organization. It is related to the pragmatic goals of an organization and to its cultural surroundings. Creating, changing and influencing this process of commitment is subject to designed communicational processes.

An established process of ethical communication in organizations is the link between otherwise contrary principles of management:

- Integrity based management versus compliance based management,
- Managerial approach versus communicational-oriented approach,
- Management of strategic impetus versus management of social equivalent.

An economical consistent concept of cultural values-management faces challenges in an inhomogeneous set of values (which is especially given in internationally operating companies). A balance of "value commitment" and the "space" that is needed for innovation is hard to establish. Yet it is crucial for the success of a company – and an integral part of an organization's value.

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