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Structured Abstract

Purpose: This chapter reviews the challenges faced by top management teams as they strive to create corporate cultures that combine a high performance with a strong sense of integrity.

Methodology/approach: The paper integrates diverse theories from organizational research and cognitive psychology, as well as published accounts of ethical breakdowns, to shed new light on the barriers to corporate integrity.

Findings: The paper distinguishes between two major types of ethical breakdowns.

Conscious transgressions, where the individuals know what they should or should not do, but choose nonetheless to follow the unethical path, a decision that they then need to rationalize and which often places them on a slippery slope.

Unconscious transgressions, where the individuals do not even realize that they are making an inappropriate decision, as they fall prey to ethical fading or to other cognitive biases.

Practical implications: The paper proposes that top management plays a key role in: establishing a climate where employees can speak up; emphasizing the importance of all stakeholders; and investing in training to increase awareness of the cognitive biases that support transgressions.

Social implications: The paper recommends that management educators must: alert students more forcefully to the personal and organizational repercussions of "minor" ethical transgressions; increase student awareness of key cognitive concepts, including ethical fading and other mental biases; and highlight the possible dysfunctions of intuitive remedies, like incentives or rules and regulations.

Originality/value of paper: The paper provides a clearer analysis of the causes of ethical breakdowns, allowing for more effective prevention.

Paper type: General Review

Keywords: Leadership, culture, integrity, performance, ethical breakdowns, transgressions.

Full Abstract

This chapter reviews the challenges faced by top management teams as they strive to create corporate cultures marrying a healthy search for performance with a strong sense of integrity. I present and discuss two major types of ethical breakdowns. In some cases, individuals know what they should do – or not to do – but choose nonetheless to follow the unethical path, a decision that they then need to rationalize and which often places them on a slippery slope. More frequently, individuals will not even realize that they are making an inappropriate decision, as they fall prey to ethical fading or to any of a variety of cognitive biases. I review possible interventions to improve the situation, including some well-intentioned but counter-intuitively dysfunctional approaches. I conclude with a few implications for practice and for educators.

Modern organizations – for profit or not – face increasingly high demands for performance. In the case of for-profit organizations, these demands come from or are exacerbated by increasingly global financial markets, where capital can flow relatively easily to greater returns elsewhere. Not-for-profits also face increasing demands for effectiveness and efficiency, from financially-strapped governments, demanding tax-payers/citizens and/or from donors hoping to obtain more impact from their contributions.

The search for the secrets of high organizational performance has hence been intense for decades and has yielded a number of well-known books along the way, some of which have stood the test of time better than others.

The search for high integrity in organizations is probably a slightly more recent phenomenon but has clearly intensified over the last few years. In part, this intensification is due to increasing expectations from society and customers, which have often led to increased regulation (including much higher fines) and lower tolerance for behavior perceived to be unethical or otherwise inappropriate. Transgressions are also harder to hide, as employees increasingly have (regulation-supported) incentives and means to speak up. And once identified (thanks to employee support or not), transgressions are likely to be disseminated much more quickly and pervasively than before – via the power of the internet, social media and even traditional media – thus having a much greater impact on employee reputation than before.

Senior leaders hence look for ways to boost both "performance" and "integrity" and, ideally, to embed them into the "culture" of the organization so their effect remains high beyond the existing leaders' tenure and focus.

Organizational culture

It is now generally accepted that organizations that enjoy lasting success do so in part because they have developed a "strong" and "positive organizational culture".

> While there will always be some counter-example, evidence provided by management thinkers like Kotter and Heskett (1992), Collins and Porras (1994) and O'Reilley and Pfeffer (2000) strongly suggests this is indeed the case.
>
> Many well-known organizations certainly also seem to believe so: General Electric, for example, explained in its 2008 Annual Report – and still features on their web site in January 2012 – that "at GE, we consider our culture to be among our innovations. Over decades our leaders have built GE's culture into what it is today – a place for creating and bringing big ideas to life. Today, that culture is the unifying force for our many business units around the world." (General Electric, 2012)
>
> Similarly, Schein (2008, p. 362), a life-long student of organizational cultures, believes that, "It can be argued that the only thing of real importance that leaders do is to create and manage culture, that the unique talent of leaders is their ability to understand and work with culture", and that "what distinguishes leadership from management (…) is that leaders create and change culture".

But what is organizational culture, exactly? Discussing the culture of an organization with its employees and managers is often a frustrating exercise in part because while we all understand the word "culture", we often understand it differently. Try this exercise: ask a group of executives what they understand by "culture". You will likely get a long list of words that while related, mean very different things!

At its most basic, culture is said to be "the way we do things around here". More sophisticated definitions include the following:

> "A pattern of shared basic assumptions that the group learned as it solved its problems (…), that has worked well enough to be considered valid and, therefore, to be taught to new members as the correct way to perceive, think and feel in relation to those problems." (Schein, 1992, p. 9)

> "The specific collection of values and norms that are shared by people and groups in an organization and that control the way they interact with each other and with stakeholders outside the organization." (Hill and Jones, 2001, p. 68)

> "The set of shared mental assumptions that guide interpretation and action in organizations by defining appropriate behavior for various situations." (Ravasi and Schultz, 2006, p. 437)

My own favorite definition is that of Goffee and Jones (1998, p. 15): "Culture comes down to a common way of thinking, which drives a common way of acting". This definition captures the fact that culture is about the way people *think*, translates into the way people *behave*, and that culture refers to a pattern of behavior that is reasonably *pervasive* throughout the organization (which can mean across countries, functions, departments, hierarchical levels and across time).

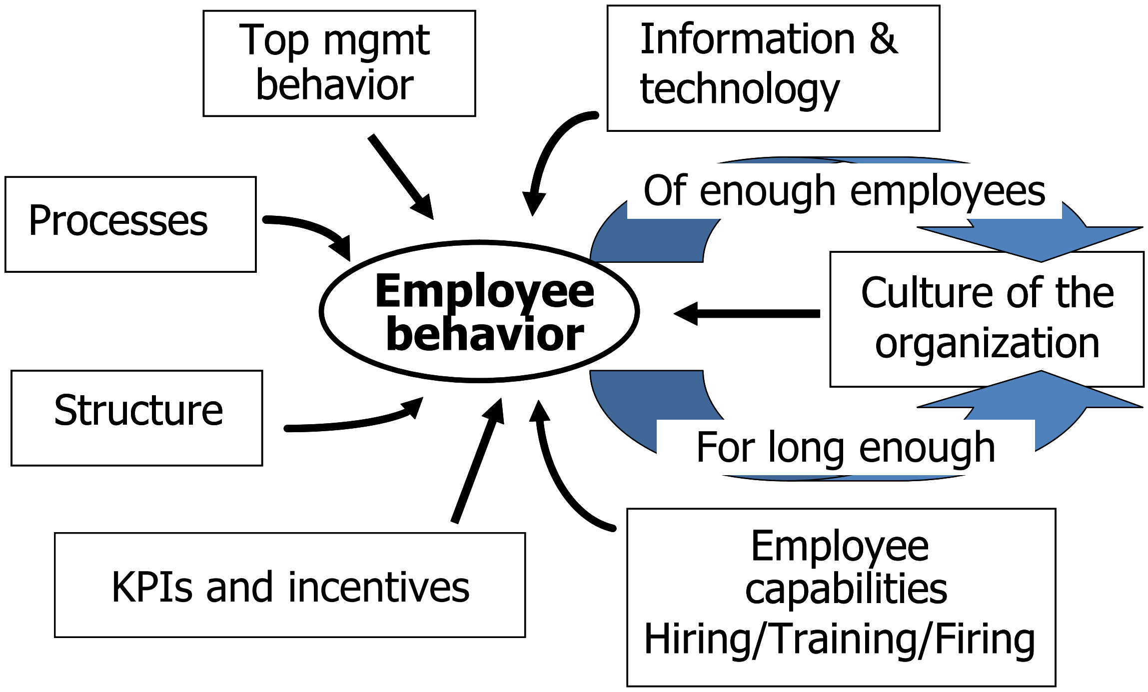
Changing an organization's culture hence requires modifying the "common way of thinking" of its members. As a result, many organizations have over the years launched "cultural change programs", where the goal was to modify employee attitudes. Such efforts tend to fail because they miss a counter-intuitive but long-known aspect of human functioning: Human beings tend to act their way into new attitudes much more than they think their way into new behaviors.

This is not a recent discovery: In his *Nicomachean Ethics,* written almost twenty five hundred years ago, Aristotle explained that "we do not act rightly because we have virtue or excellence, but we rather have those because we have acted rightly." He explained that human beings "acquire a particular quality by constantly acting a particular way... Moral excellence comes about as a result of habit. You become just by performing just actions, temperate by performing temperate actions, brave by performing brave actions."

Re-shaping the culture of an organization hence requires *reshaping the behavior of enough people, for long enough* for them to *internalize the new behavior, i*.e., for the new behavior to become "a habit".

I discussed in previous EIASM workshops (Manzoni, 2006, 2008) how re-shaping employee behavior requires the alignment of the signals sent by all the managerial levers to which employees are exposed. There are several ways to describe such levers. Pascale and Athos (1981) provided a model emphasizing Seven Ss (Strategy, Structure, Systems, Skills, Staff, Style and Shared values). Galbraith (1995) proposed the "Star Model", featuring strategy, structure, process, rewards and people. I tend to use a slightly different framework, presented in Figure 1.

Figure 1
Re-shaping an organizational culture



These levers must send consistent enough signals, and must do so for a long enough period for employees to internalize the new behavior. How long is long enough depends on a number of endogenous and exogenous factors, including how large the required change is, how deeply anchored are the previous behaviors, how individually powerful and collectively aligned are the forces applied to the employees, how many individuals need to be affected, how geographically dispersed these individuals are and how easy it is to monitor behavior and enforce the changes. But it typically takes years rather than months or weeks for people to a) learn effectively to produce new behaviors that are significantly different from their initial programming, b) perfect this learning to a high enough degree for the new behavior to become a habit.

Tesco - the British-based but increasingly international retailer - provides a fantastic illustration of this alignment process. As discussed in Barsoux and Manzoni (2008), Tesco deploys a series of organizational practices and mechanisms that are often individually smart but rarely earth-shattering; most organizations do most of what Tesco does most of the time, but very few do all of it all the time over several years. Tesco has enjoyed exceptional success over the last fifteen years and has created a remarkable corporate culture characterized by high employee engagement, customer focused innovation and excellence in execution because its managerial levers are:

- Incredibly *aligned*, with the organization's strategy and with one another.
- Applied with *great intensity* (i.e., people do not just "do things" to "tick the box" and satisfy the process requirements; they really invest time and energy into the activity).
- *Consistent over time*, driven by a management team that has been together for over a decade.

High Performance, High Integrity

I will not focus too much here on the "high performance" side of this equation, as I have done so before (Manzoni, 2002, 2004, 2006). High performance tends to be an elusive characteristic that rests on a large set of factors that are not always equally present. Still, companies that outperform their peers over non-trivial periods of time tend to:

- Propose products and services that are highly valued by customers and consumers (i.e., the products and services are perceived to provide great value for their price);
- Have effective and efficient enough operational and managerial processes to capture some of the value created for customers;
- Display a strong performance orientation, typically characterized by the setting of demanding objectives and their pursuit with great focus, energy and intensity.

The "high integrity" side of the equation is no simpler. High Integrity starts with a basic *compliance* dimension, whereby the organization's (direct and indirect) employees respect the laws and regulations that apply to their activities. That's of course a necessary condition, but it is by no means a sufficient one. High Integrity requires more than respecting laws and regulations. It implies that the organization's direct and indirect employees will do "the right thing" for the organization's various constituencies , including customers, employees, suppliers, communities and society in general.

The definition of the "right thing" is by no means clear-cut nor is it necessarily consistent over time and across countries and industries. Still, I think it is fair to say that as a general rule and across the world, society has over the last few years become increasingly demanding vis-à-vis organizations, in terms of their physical and social impact on communities, the appropriateness of certain business practices or the distribution of wealth between shareholders, managers and employees.

Different organizations (operating in the same industry and country) may also argue that "the right thing to do" is different for them than for their competitors. To some extent, expected behavior indeed depends on the organization's brand proposition and the reputation it wants to create for itself. (For example, Tesco has over the years worked hard to be perceived on the side of consumers and more recently on the side of communities. Banks have more rarely taken such a stand, but now that Standard Chartered Bank has forcefully communicated it's new "Here for Good" tag line, it is likely to be held to a higher standard than some of its competitors that have not made such a promise.)

The factors underlying organizational performance are probably too numerous and feature too much lag and measurement-error for us ever to get an uncontroversial answer to the question: What is the long-term relationship between High Performance and High Integrity? There is a certain amount of anecdotal evidence suggesting that over the long run this relationship is generally positive. Studies such as Kotter and Heskett (1992) or Collins and Porras (1994) go in that direction too.

It is increasingly clear that breakdowns in integrity can be extremely costly. Financial service organizations such as UBS and Société Génerale have also suffered considerable losses because of employee misconduct. The disappearance of companies like Enron, Parmalat or WorldCom also involved inappropriate behavior and cover-ups. And of course regulators have recently been levying significant fines – in excess of $1 billion – on companies such as Pfizer, J&J and Siemens, to name but a few.

Conversely, some organizations have managed to create significant goodwill for themselves with their key constituencies and this goodwill can help reduce the negative consequences of an isolated breakdown.

In the short term, however, there can be clear conflicts between the requirements of performance and integrity: a price increase can destroy customer goodwill but lead to a short-term improvement in profit; employee goodwill can be depleted by withholding compensation or investments in safety or training, with negative longer term consequences but a positive impact on short-term financial performance.

Arguably, though, these trade-offs are at the heart of managers' jobs. Most managerial decisions involve some form of trade-off: more focus on one activity leaves less time for another activity; more attention to the urgent can lead to less attention to the important; an investment here will preclude an investment there. Managers operate under conditions of scarce resources – time, attention, money – and hence need to allocate these resources in one direction at the expense of another.

Similarly, a great many managerial decisions involve trade-offs between short-term and long-term financial performance. In the absence of short-term financial objectives, most organizations could make much larger (and not necessarily long-term NPV enhancing) investments in increasing the satisfaction of their customers, suppliers, employees, or to improve their social and environmental performance.

These trade-offs are hard to assess because of the same two reasons that make possible the divergence between short and long term performance: a) imperfect – i.e., incomplete – measures of performance that capture the impact of managerial decisions with some lag, b) managers' always imperfect understanding of cause-effect relationships underlying long-term performance. The divergence can then be magnified by offering managers incentives that are tied to short-term performance measures.

Management accounting and control scholars have proposed ways of addressing this challenge. Many authors have emphasized different aspects, but overall the prescription would include:

- The development and use of multiple and more sophisticated indicators of performance, to:
    - Help managers better understand over time the cause-effect relationships involved (and thus make better short-term – long-term trade-offs).
    - Propose incentives tied to more complete and more long-term friendly objectives.
- The development of a "control system" that following the work of Simons (2000) and others, might include:
    - A belief system featuring corporate values, leadership competencies and/or a Code of Conduct, to inspire employees to "do the right thing".
    - Boundary controls featuring significant numbers of regulations and policies, accompanied by employee training and certification, with audits to check compliance by an independent group of specialized employees.

I will argue below that these prescriptions are insufficient and, in some cases, can be counter-productive.

In summary, the challenge of creating High Performance – High Integrity organizations and corporate cultures requires top management to strive to create a common way of thinking which drives a common way of acting, such that (tens of) thousands of managers and employees – coming to the matter with different personal norms and often different cultural norms – will become willing and able to respect the law and, more generally, to "do the right thing" for a complex set of stakeholders sometimes presenting divergent needs.

Integrity breakdowns

Conscious breakdowns

In order to understand how to create such a culture, let us first examine why the employees of an organization would fail to "do the right thing".

One obvious reason is that employees face some motivation to misbehave. There are two major drivers: fear and greed.

The greed factor is clear: Employees sometimes try to take advantage of the imperfections of performance measures and/or of the control system to take actions that enhance their own welfare (e.g., expected compensation) at the expense of other stakeholders and potentially of the organization's long-term reputation and/or performance. While one can never be sure of individual motivations, the behavior of David Sokol (a Berkshire Hathaway senior executive who bought a company's stock very close to the time he recommended the stock to his employer and then realized a multi-million dollar profit (when Berkshire Hathaway bought the company a few weeks later), as described in Barrett (2011), could reasonably be attributed to a desire for personal enrichment.

The other major driver of "unethical behavior" is fear. This fear – of losing relationships, money, promotion opportunities or personal reputation if one does not engage in the unethical behavior – is often self-imposed by the employee. It is rooted in the individual's understanding of what the boss expects or desires, and what the boss, the organization or relevant others are likely to value.

Of course, in some cases the boss or relevant others can reinforce the employee's perception of their preferences through their behavior. Employees tend to be sensitive to what their bosses say and do (e.g., explicit references to a clear link between achievement of some performance level and some reward or punishment). But employees also notice what their bosses do *not* say or do (e.g., the failure to mention that these performance objectives ought to be met through behavior that meets certain ethical criteria).

Managers and organizations must understand just how little encouragement is needed for most reasonable human beings to perform acts that they know to be problematic. This human propensity was vividly demonstrated by Milgram's famous (1963, 1974) experiments, in which the vast majority of subjects – with minimal pressure being exerted on them – agreed to administer electrical shocks of very high intensity to other individuals, regardless of the apparent pain experienced by recipients. These experiments have since been replicated in numerous countries over the years, including over the last few years on TV programs in the UK, France and the US, with surprisingly consistent results across countries and decades.

The lesson is: Human beings the world over have a strong propensity to conform to the wishes of credible and legitimate authority figures. In most national and corporate cultures, bosses are seen as such figures and must hence be very mindful of the signals they send – and fail to send.

Having succumbed to fear and/or greed and committed actions that they know to be problematic, employees then need to rationalize these actions, i.e., to explain to themselves that while the action would normally be inappropriate, it is actually permissible under the circumstances. This rationalization process can take a number of forms, including:

- Minimizing the magnitude of the breach: "Yes it was inappropriate, but it's a very small breach."
- Comparing to other offenders: "Others are doing it too – and started doing so before me."
- Attributing the breach to an unavoidable/ external cause: "I did not really have a choice; "they"/this made me do it."
- Attributing the breach to a higher purpose: "If I had not done this, worse outcomes would have occurred – e.g., the organization would have gone bankrupt and many people would have lost their jobs."

Research shows – and our own human experience every day confirms – that the human tendency to rationalize is considerable. This propensity is based on the human need to reduce cognitive dissonance, i.e., to reduce or eliminate the tension that people experience when they hold two cognitions that are psychologically inconsistent, such as "I'm a highly ethical person" and "I just committed an action that I would normally regards as inappropriate".

Human beings' propensity to reduce cognitive dissonance was first studied and analyzed by Festinger (1957). Since then, a considerable number of studies have documented the pervasiveness and robustness of this phenomenon. In particular, many studies show that human beings can be remarkably resistant to the existence of accurate and relevant disconfirming data. This empirical regularity is explained by recent neuroscience studies. MRIs of the brain show that when people are exposed to dissonant information, reasoning areas of the brain shut down. By contrast, when exposed to consonant information, emotion circuits of the brain light up as if the subject was experiencing a pleasurable sensation. (Westen, Blagov, Harenski, Kilts and Hamann, 2006)

Studies of individual and corporate wrongdoing also suggest that misbehavior tends to increase over time. The individual engages on a "slippery slope" by committing a small ethical breach, which leads to a larger one and another… As Cynthia Cooper, the whistleblower in the WorldCom accounting misreporting, explained it in her (2008) account of the debacle: "People don't wake up one day and say, "I think I'll become a criminal today." Instead, it's often a slippery slope and we lose our footing one step at a time."

Cooper's (2008) account offers a fascinating insight into the incremental and social nature of such corporate misbehavior. At the time, WorldCom was a fast-growing and exciting place to work. The darling of Wall Street, it had built on very humble beginnings and was in the process of conquering the US's telecom world. Headquartered in a small town in the South of the US, it was the most glamorous and desirable employer around as well as a source of local pride.

The end of a quarter revealed an unexpected shortfall in quarterly profits. Communication of that shortfall would likely have a significant negative impact on a stock price that rested on very lofty growth expectations by the market. A reduction in the stock price would in turn hamper the continued growth of WorldCom, which was financing most of its acquisitions by issuing more stock. Three accountants were asked to investigate the spike in expenses and could not explain it. They were then asked by their charismatic boss – a smart, energetic, hard-working, engaged and engaging professional – to "make it go away".

The individuals knew that what they were being asked to do was inappropriate. They considered refusing to comply, but ultimately relented. They "sharpened the pencil" and reduced various reserve accounts to make up for the shortfall. They also prepared their letter of resignation, which they were prepared to hand in if their boss did not agree to issue a clear indication to Wall Street that future growth would be slightly reduced. The CFO made the announcement and the letters of resignation stayed in the drawers. The individuals figured that this was a small breach – it was almost like a "bridge loan", which would be re-paid next quarter – committed for a good cause – the protection of a great company's growth prospects… a small price to pay not to let down one's friends and "corporate family". As the next quarter progressed, memories of the emotional tension experienced at the time started to fade.

Unfortunately, the end of the next quarter proved problematic as well. The quarterly profit was again below expectations… The three accountants again agreed to find the required amounts in various reserve accounts. In time, they exhausted all the reasonable reserve accounts and had to resort to more aggressive techniques to cover up the misreporting: they started capitalizing items that should have been considered current expenses.

Of course, the individuals' discomfort increased with the magnitude and severity of the cheating; they grew increasingly uncomfortable with their actions. But by then, their initial motivation to collude – their desire not to let down their "corporate family" and in the process lose a job they loved in a company they loved – was now supported by another motivation. If they stopped now, their past ethical breaches would become public and would have devastating consequences for them and their families. They were – and clearly felt – trapped.

Cooper (2008) cites two classic thinkers on this notion of a slippery slope:

- From Scottish author Samuel Smiles: "Sow a thought, reap an action; sow an action, reap a habit; sow a habit, reap a character; sow a character, reap a destiny."
- From C. S. Lewis: "Every time you make a choice, you are turning the central part of you, the part that chooses, into something a little different than it was before… Good and evil both increase at compound interest. That is why the little decisions you and I make every day are of such importance."

Cooper concludes that "the foundation of our character is laid brick by brick, decision by decision, in how we choose to live our lives" (2008, p. 364).

One could argue that these individuals lacked courage. Gebler (2006) indeed reports quotes from them suggesting that they would agree with that statement.

- "I'm sorry for the hurt that has been caused by my cowardly behavior."
  -- *Scott Sullivan, CFO*

- "At the time I consider the single most critical character defining moment of my life, I failed. It's something I'll take with me the rest of my life."
  -- *David Myers, controller*
- "Faced with a decision that required strong moral courage, I took the easy way out… There are no words to describe my shame."
  -- *Buford Yates, director of general accounting*

One response would hence be that organizations need to hire individuals who because of their character and personality are more likely to display ethical and courageous behavior. Many studies of high performing organizations indeed tend to suggest that great companies do invest more time, effort and energy in selecting the "right people for them".

But in fairness, the individuals engaged in the WorldCom debacle were not known to be especially weak. As described by Cooper, who knew them well, they were basically "good people" who made bad decisions. They took a first action that breached their principles and rationalized it away. This first ethical breach made it easier to commit a second one, at which point they became almost condemned to continue lying in order to conceal their initial transgressions.

Unconscious breakdowns

Fear of hypothesized consequences and/or a desire to improve one's welfare can hence lead employees and managers to set aside their principles and knowingly fail to do "the right thing". In many cases, however, employees and managers fail to do the right thing because they simply do not know what is "the right thing to do".

In some cases, people can identify that they face a dilemma but find it difficult to weigh the various parameters of the decision. But recent research shows that in many cases, people do not even realize they are facing an ethical issue; as a result, they often fail to recognize that they (and/or others) are behaving unethically, which also leads them to over-estimate their own (and their favored others') integrity.

There at least four major causes to this blindness:

"Ethical fading"

Ethical fading refers to the process by which the ethical aspects and/or implications of the decision fade away from our mind; we fail to notice them. Research (see Bazerman and Tenbrunsel, 2011a) shows that ethical fading is more likely to happen when:

- The "business" implications of the decisions are heavily emphasized (as they would typically be in any resource-constrained environment).
- Language euphemisms are used (e.g., referring to "aggressive" accounting practices, "let go" for "fire", or "right sizing" for "mass sackings").
- Potential victims are numerous and anonymous (as opposed to an individual who can be identified).

More worryingly, research shows that some of the counter-measures proposed in "mainstream ethical programs" may also contribute to ethical fading. Studies suggest that the following conditions can trigger an *increase*, rather than decrease in ethical fading and unethical behavior:

- Small financial penalties associated with transgression
    - Several laboratory experiments (e.g., students facing an environmental decision, in Bazerman and Tenbrunsel, 2011a) and field experiments (e.g., parents showing up late to pick up their child at day care, in Frey and Jegen, 2001) show that the presence of a penalty leads people to feel that paying the penalty discharges them from any other responsibility. The decision is no longer an ethical one, it becomes a business decision.

- The existence of a large number of rules and regulations
    - Many "ethics and compliance" programs feature large numbers of rules and regulations. This number also tends to increase over time, as new challenges get identified in some part of the organization and the organization feels the need to regulate this point throughout its ranks.
    - Unfortunately, research in psychology (Self-Determination Theory, Deci & Ryan, 1985) and economics (Motivation Crowding Theory, Frey & Jegen, 2001) shows that this tactic is likely to backfire. Several experiments indeed document an association between a large number of rules and regulations and an increase in transgressions. It seems that large numbers of rules and regulations lead individuals to feel that they no longer have to self-monitor; the monitoring is externalized to the (seemingly exhaustive) rules and regulations. The question then ceases to be, "Is this the right thing to do?" and rather becomes, "Is this allowed?"
- Disclosure of the "conflict of interest"
    - The idea of requiring individuals to disclose conflicts of interest seems quite reasonable. Awareness of this conflict of interests should make other interested parties more cautious in their dealings and more wary of the conflicted party's estimates. In an interesting experiment, however, Cain, Loewenstein and Moore (2005) showed that third parties are not always able to discount the effects of the conflict of interest appropriately. More interesting still, they found that individuals asked to disclose their conflict of interest provided estimates that were more biased than those who faced the same incentives but did not disclose this conflict of interest to the estimates' recipients. Again, this result is consistent with a decrease in self-monitoring by individuals who feel that disclosing their conflict of interest discharges them of their responsibility to be accurate.

Motivated blindness

Motivated blindness refers to human beings' tendency to selectively disregard information that would be costly for them to notice and to interpret available information in ways that are supportive of their best interest. This includes observation and interpretation of others' behavior, i.e., human beings' propensity not to notice others' unethical behavior when noticing it would potentially harm the observer.

Moore, Tanlu and Bazerman (2010) ran an interesting experiment in this area, when they asked 4 groups of individuals to estimate the value of a fictional company. Each group was given a role in the potential transaction: buyer, seller, buyer's auditor and seller's auditor. The two groups of auditors were asked to act as independent experts and were rewarded based on the accuracy of their estimate. As expected, "sellers" provided higher estimates of company value than "buyers". More surprisingly, sellers' auditors also provided higher estimates – 30% higher on average! – than buyers' auditors. This study was replicated with actual auditors from one of the Big Four. The outcome was similar, confirming that even in the presence of incentives encouraging the impartial behavior they were being asked to adopt, the "auditors" were unconsciously influenced by the point of view of the party by whom they were supposedly being hired.

Confirmatory biases

A considerable body of work in the psychology literature documents how human beings' perception of reality is shaped by their beliefs and expectations. In particular, we are prone to selecting, interpreting and even remembering events in ways that are consistent with our beliefs. At a conscious level, this process is a manifestation of Festinger's (1957) observation that human beings need to reduce cognitive dissonance.

But very often this filtering process will be totally unconscious, i.e., will occur without the individual noticing it. The dissonant information (dissonant because contradicting our view or simply because unexpected) will simply not print on our radar screen! If it does appear on the radar screen, it will often – and in complete good faith – be interpreted in ways that are consistent with our belief/expectation.

And while for decades we thought that memory, at least, was a reliable companion, recent research shows that memory is far less reliable than previously thought. As Tavris and Aronson (2007, p. 6) put it: "Memories are often pruned and shaped by an ego-enhancing bias that blurs the edges of past events, softens culpability and distorts what really happened." Evidence on the imperfections of human memory has grown to the point that the US police and justice system is actively re-examining the role and influence of eyewitnesses (see Liptak, 2011).

So going back to the David Sokol example mentioned above, Bazerman and Tenbrunsel (2011b) examine Warren Buffett's failure to understand the inappropriateness of David Sokol's action and attribute it to motivated blindness. I think confirmatory biases are at least as good an explanation. David Sokol did tell Warren Buffett that he owned some stock in the company they were discussing. And I am absolutely willing to buy that Warren Buffet never thought of asking Sokol, "And when did you buy that stock?" I think it did not even cross Buffett's mind that Sokol bought the stock a few days before! Sokol was one of his trusted lieutenants; ethical behavior is an important pillar at Berkshire Hathaway; Buffett had no reason to suspect foul play and likely made an immediate and unconscious assumption on the timing of the purchase.

The unconscious nature of this process is important, because unconscious processes are harder for human beings to observe and hence correct. Unconscious biases are also a lot more pervasive than we tend to think. For example, when asked if they are prejudiced based on others' race, age or weight, most individuals will respond negatively. When tested in ways that do not rely on introspection and instead tap the individuals' unconscious processes, however, many individuals turn out to be more prejudiced than they thought. (See Greenwald, McGhee and Schwartz's (1998) study on the Implicit Association Test, and the body of work that it has spawned over the last 13 years).

Self-serving bias / Identity protection

Much evidence supports the idea that most human beings want to have a positive image of themselves. Studies have identified a "better-than-average effect", also called "illusory superiority", which leads a vast majority of people to rank themselves as above average in a variety of dimensions including driving skill, social sensitivity, leadership ability and many other attributes. (See for example, Kruger, 1999; Roese and Olson, 2007; and Suls, Lemos and Stewart, 2002). Human beings are also vulnerable to the widespread self-serving bias, which leads them to attribute their success to their merits and internal dispositions but their failures to unfavorable external factors (see Miller and Ross, 1975).

This desire to maintain a positive image can also lead us to regard as acceptable, when performed by us, actions that we otherwise know to be problematic. DeSteno and Valdesolo (2011) thus report on a study that asked people to allocate between themselves and another party two tasks: a short and rather pleasant one, and a longer, less pleasant one. The other party would not know who assigned the task to them.

In a first test, a group of individuals was asked what would be the fair and ethical thing to do. A vast majority of people indicated that the decision makers should allocate the long and difficult talk to themselves. Another (similar) group of individuals was then faced with that choice, and a vast majority of people chose to allocate the short, easy task to themselves. They then rated their actions as perfectly fair and ethical, thus displaying a clear double-standard.

The study then went one step further. Individuals were given wristbands of one of two colors, and asked to watch an individual from their group or from the other group, go through the exercise and assign him or herself the easy task. Even though observers had no personal stake in the outcome, the color of their wristband was enough to bias their judgment. Their assessment of the action was colored – literally! – by the wristband, with observers tending to rate the action as appropriate when the wristband was the same color as theirs, but decidedly less ethical if the individual wore a different color wristband.

So just as human beings have a tendency to extend the self-serving bias to their "in-group", we also seem to have a tendency to give the benefit of the doubt to people who are – or at least seem to be – "in our camp".

Going one step further, DeSteno and Valdesolo focused another study on the rationalization process (I am/you are a good person, so if I/you do this, it must be OK). They hypothesized that this rationalization process, while unconscious, probably consumed mental energy. So they asked another group of subjects to memorize a series of numbers and retain it in their heads as they were answering questions on the experiment and their actions. When thus kept cognitively busy, participants saw their behavior for what it was and no longer rated it as ethical, suggesting that the unconscious rationalization process requires processing and consumes mental energy.

One last comment on this front: Sachdeva, Iliev and Medin (2009) primed individuals to think of themselves as virtuous (generous, caring) or not (greedy, disloyal). In a subsequent, apparently disconnected step of the experiment, they asked participants whether they wanted to make a donation to charity. The people who wrote about themselves as virtuous ended up giving less – 5 times less! – than the people who were prompted to write about themselves in negative terms. Belonging to a group or an organization that has historically been morally upstanding might hence lead people to over-estimate their ethical "nature" and under-estimate how much effort they need to make to behave ethically. I wonder to what extent this phenomenon might have contributed to the recent series of mishaps, quality problems and associated cover-ups observed at Johnson & Johnson, a company historically recognized as a paragon of virtue (see Voreacos, Nussbaum and Farrell, 2011).

Implications for research and practice

This discussion suggests a number of possible implications for practitioners and management educators.

Implications for practice

- Be careful with intuitively appealing responses such as increasing the number of rules and regulations, imposing penalties for transgressions and relying on the requirement to acknowledge conflicts of interests. While reasonable on paper, these practices can backfire and lead to more rather than less inappropriate behavior, as the presence of external control can lead individuals to exercise less self-control.
- Invest time and energy in a massive "managerial judgment education program". Each employee and manager brings to their work their individual programming, in part shaped by their national culture and their personal prior experiences. Yet they will make decisions that engage the name and reputation of the organization. In an ideal world, they would hence be trained to internalize the set of principles and trade-offs that the organization would like them to make.
- Combat ethical fading, by making sure that managers – starting with top management – regularly emphasize the importance of all stakeholders and the fact that financial performance is the result of a job well done, rather than an end in itself.
- Create a climate where employees can speak up and express their uneasiness about the decision that is being contemplated, thereby increasing the likelihood that possible transgressions will be identified and intercepted.

Implications and questions for management educators

Working on this chapter has led me to question whether I do enough in my teaching to increase managers' capabilities on the ethics/integrity front. For example, instructors might ask themselves the following questions.

- Do I highlight clearly and frequently enough for my students and executive education participants the organizational and personal costs of ethical transgressions, and the slippery slope that the initial transgression triggers?

- Does my teaching sufficiently help increase managers' and auditors' awareness of various important concepts and mechanisms discussed above, such as:
    - Ethical fading
    - Motivational blindness and confirmation biases
    - Self-serving bias
    - The dangers of intuitively appealing responses featuring more rules, regulations and incentives.

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Appendix I

Tesco's model (as described in Tesco's 2009 Annual Report)

Tesco's long-term strategy

- To be a successful international retailer
- To grow the core UK business
- To be as strong in non-food as in food
- To develop retailing services
- To put community at the heart of what we do

The basic model

- Our **core purpose** is to create value for customers to earn their lifetime loyalty
- **Our success depends on people**: the people who shop with us and the people who work with us
  - If our customers like what we offer, they are more likely to come back and shop with us again
  - If the Tesco team find what we do rewarding, they are more likely to go that extra mile to help our customers
- Hence our **two values**
  - *No-one tries harder for customers*
  - *Treat people as we like to be treated*

This model rests on four major thrusts:

A great place to work

Our staff have told us what is important to them:

- To be treated with respect,
- Having a manager who helps them,
- Having an interesting job, and
- Having an opportunity to get on.

Treat people how we like to be treated

The way we work

- We deliver consistently every day,
- We try to get it right first time,
- We make jobs easy to do,
- We know how vital our jobs are, and
- We always save time and money.

Better for customers, Simpler for staff and Cheaper for Tesco.

Shopping trip

Customers have told us they want:

- Clear aisles,
- To be able to get what they want,
- Good prices,
- No queues, and
- Great staff.

No one tries harder for customers

Our community

- Actively supporting local communities,
- Buying and selling our products responsibly,
- Caring for the environment,
- Giving customers healthy choices, and
- Good jobs for local people.

Together we can make a difference

Tesco's "Steering Wheel" (the measurement tool the company uses to report, analyze and reward performance) reflects these four thrusts as well as Tesco's long-term strategy.

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