THE STATE OF ETHICS IN LARGE COMPANIES

*When the largest companies invest resources
in ethics and compliance, they get impressive results.*

ERC

Ethics Research Center

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A Research Report from the National Business Ethics Survey® (NBES®)

The National Business Ethics Survey® (NBES®) generates the U.S. benchmark on ethical behavior in corporations. Findings represent the views of the American workforce in the private sector. Since 1994, the NBES and its supplemental reports have provided business leaders a snapshot of trends in workplace ethics and an identification of the drivers that improve ethical workforce behavior. With every report, ERC researchers identify strategies that business leaders can adopt to strengthen ethics cultures.

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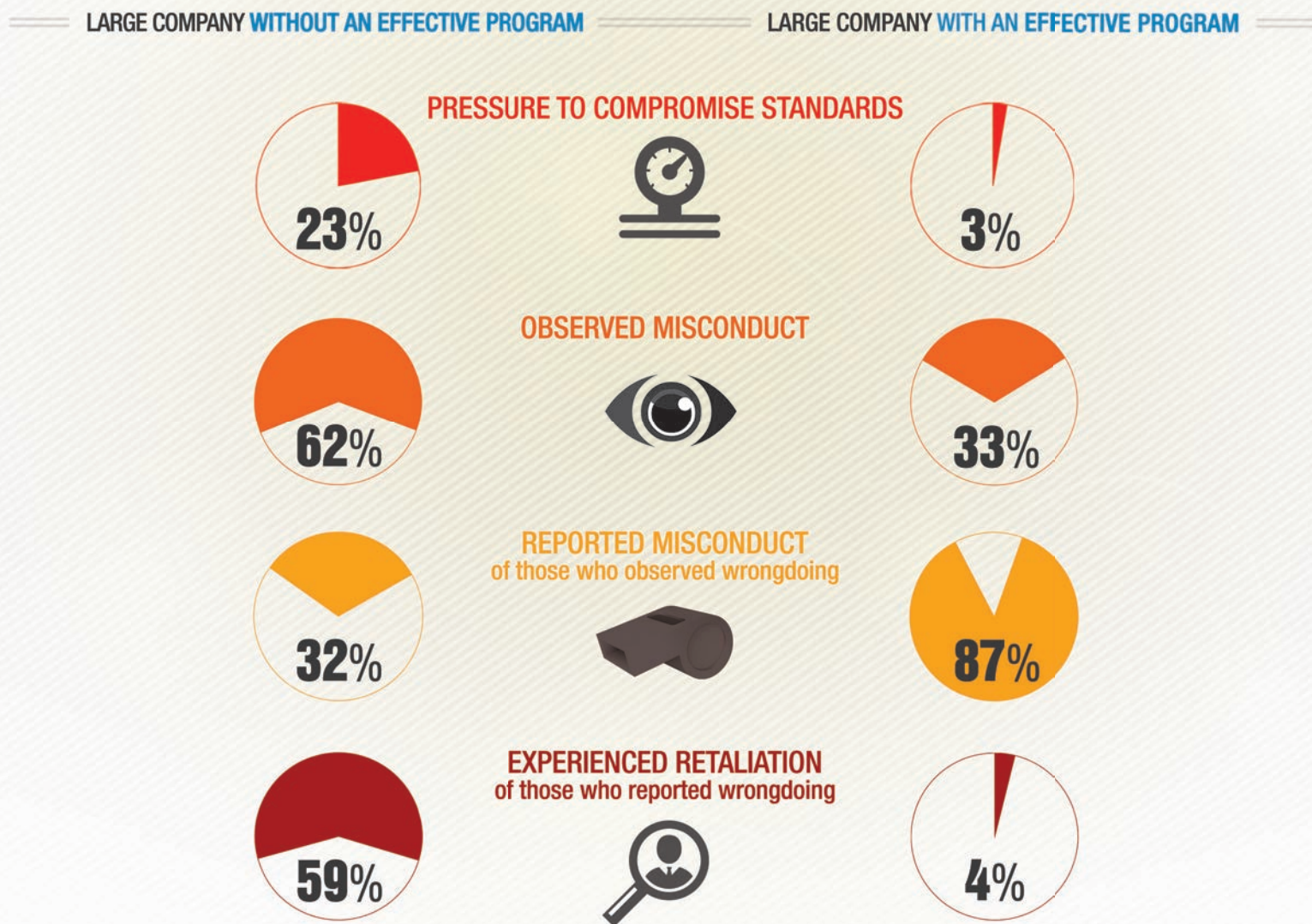and is made possible in part by support from our sponsor:

CENTER FOR **AUDIT** QUALITY

When the largest companies (those with 90,000 or more employees) invest resources in ethics and compliance, they get impressive results. The strength of a company's ethics culture and the effectiveness of its internal ethics and compliance (E&C) program are closely tied to workplace behavior. Each key indicator of ethical performance - pressure to compromise ethics standards, observation of misconduct, reporting of violations, and retaliation for reporting - improves in large companies with strong ethics cultures. Ethical performance is strengthened in companies with effective E&C programs. In fact, pressure and retaliation become extremely rare in the largest companies when they implement effective ethics programs.

Pressure to violate standards and misconduct decline substantially; workers are far more likely to report the misconduct they see; and they are far less likely to face retribution for reporting when companies have effective E&C programs. Only one-third (33 percent) of workers observed misconduct in large companies with effective ethics programs, compared to a misconduct rate of almost 51 percent among all large companies and more than 62 percent for large companies that do not have effective E&C programs. Pressure and retaliation fall to extreme lows (3 percent and 4 percent, respectively) in big companies that have established effective E&C programs.

LARGE COMPANY **WITHOUT AN EFFECTIVE PROGRAM**   LARGE COMPANY **WITH AN EFFECTIVE PROGRAM**

PRESSURE TO COMPROMISE STANDARDS

23%   3%

OBSERVED MISCONDUCT

62%   33%

REPORTED MISCONDUCT
of those who observed wrongdoing

32%   87%

EXPERIENCED RETALIATION
of those who reported wrongdoing

59%   4%

THE STATE OF ETHICS IN LARGE COMPANIES

The impact of effective E&C programs at large companies is remarkable. Every one of the four key measures of ethical performance is markedly better in companies with effective programs. Employees in large companies with effective programs feel less pressure to compromise standards, observe misconduct at lower rates, report misconduct at higher rates, and experience less retaliation for reporting misconduct. Pressure to compromise ethics standards is 20 percentage points (ppts) lower in large companies with effective programs versus large companies with ineffective programs. The rate of observed misconduct is 29 ppts lower; the rate of reporting misconduct is 55 ppts higher; and the rate of retaliation for reporting misconduct is 55 ppts lower.

Reduced pressure to compromise ethics standards and retaliation, as well as increased reporting, are critical to reducing an organization's ethics risk. The level of pressure is important because when pressure decreases, so does the potential for wrongdoing. Reducing retaliation matters because the fear of retribution discourages reporting. Reporting tends to boost ethical performance because it creates an opportunity to fix problems. When misconduct goes unreported, on the other hand, problems can fester.

WHAT IS AN EFFECTIVE ETHICS & COMPLIANCE PROGRAM?

Comprehensive E&C programs include six key program elements[1]:

1. Written standards of ethical workplace conduct;

2. Training on the standards;

3. Company resources that provide advice about ethics issues;

4. A means to report potential violations confidentially or anonymously;

5. Performance evaluations of ethical conduct; and

6. Systems to discipline violators.

A seventh element is a stated set of guiding values or principles.

NOTE: The study cited here did not include an in-depth investigation of these elements and their impact.

Effective E&C programs are vital, living parts of a company's ethos and way of doing business. Effective programs ensure that ethical conduct is rewarded and that employees know how to uphold ethics standards in their work and feel supported in their efforts. ERC measures six hallmarks of a company with an effective ethics and compliance program:

1. Freedom to question management without fear;

2. Rewards for following ethics standards;

3. Not rewarding questionable practices, even if they produce good results for the company;

4. Positive feedback for ethical conduct;

5. Employee preparedness to address misconduct; and

6. Employees' willingness to seek ethics advice.

1. ERC measures these six elements, which are outlined in Chapter Eight of the Federal Sentencing Guidelines Manual. The Federal Sentencing Guidelines for Organizations also call for oversight by the governing authority, high-level personnel with overall responsibility for the program, and individuals with operational responsibility for the program.

Company culture also makes a huge difference in the way employees behave. Large companies are often stereotyped as cold or indifferent to employees. But, in truth, there can be significant variation in the strength of ethics cultures from one large company to another. Strong ethics cultures characterized by ethical leadership, supervisors who emphasize ethical behavior, and employees who value ethical conduct and accountability are among elements that invariably lead to better conduct in the workplace.

The impact of ethics culture in large companies is substantial, particularly in terms of a reduced level of misconduct. Some 42 percent of employees observe misconduct in large companies with strong ethics cultures, but nearly nine in ten (89 percent) witness wrongdoing when ethics cultures are weak. Seventy-three percent of workers in strong ethics cultures report misconduct when they see it, compared to 55 percent reporting in weak ethics cultures. And both pressure and retaliation are much less commonplace than in companies with weak ethics cultures (by 36 and 50 percentage points respectively).

IN LARGE COMPANIES STRONGER ETHICS CULTURE IS RELATED TO BETTER OUTCOMES

	WEAK CULTURE	STRONG CULTURE	NBES 2013[1]
PRESSURE	42%	6%	9%
MISCONDUCT	89%	42%	41%
REPORTING	55%	73%	63%
RETALIATION	58%	8%	21%
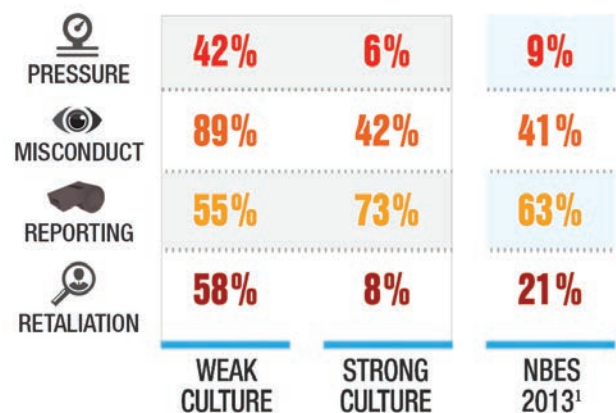
Additionally, companies with effective ethics programs and strong ethics cultures are less likely to be ones in which leadership engages in misconduct, and more likely to be ones in which misconduct happens as an isolated incident rather than as a company-wide practice. The first finding is important because leaders need to set the example for others to follow. The second is important because when companies commit to ethics, the misconduct that does occur is more likely a matter of a bad apple than a bad tree; and isolated instances of misconduct are probably easier to address than systemic patterns.

IN LARGE COMPANIES WITH EFFECTIVE E&C PROGRAMS, VAST MAJORITY OF MISCONDUCT COMMITTED BY INDIVIDUAL "BAD APPLES"

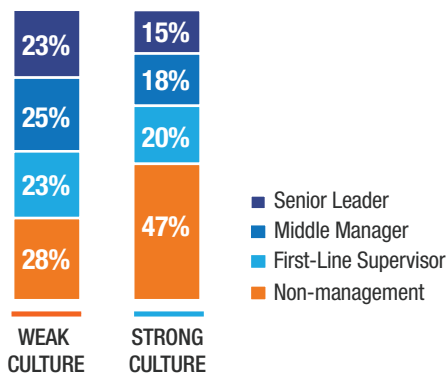|	Single Person	Multiple People	Company-Wide
Effective Program	68%	27%	6%*
Ineffective Program	26%	48%	26%
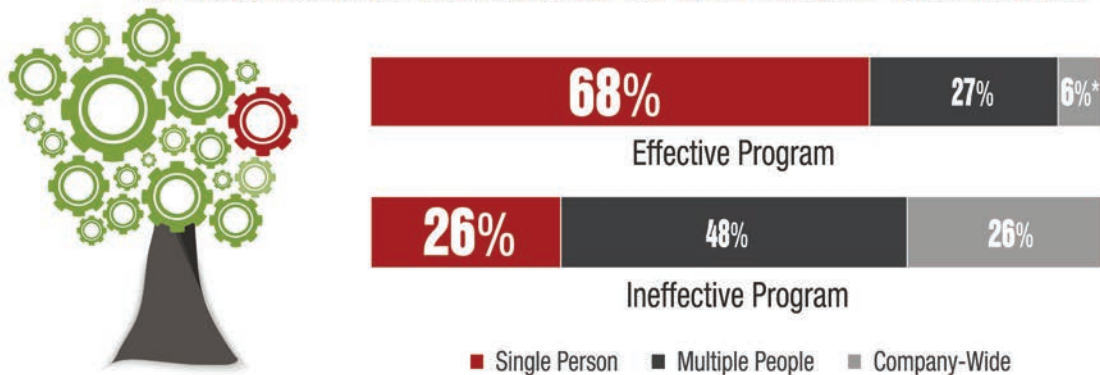
*PPT differences are calculated based on unrounded percentages.

The frequency of misconduct involving senior managers falls dramatically in large companies with effective programs. Middle managers also are much less likely to violate rules when companies have effective ethics programs. All told, the percentage of misconduct involving managers of any level dips under 40 percent when large companies implement effective ethics programs, compared to 62 percent in the absence of such programs. Isolated instances of misconduct account for a much higher share of wrongdoing – about 57 percent – in companies with effective ethics programs. That's good news because it means there are fewer systemic problems to address.

The pattern is similar in companies with strong cultures. That's not surprising because effective E&C programs help build positive ethics cultures. In weak cultures, managers are involved in 72 percent of observed misconduct. Managerial involvement falls to 53 percent in strong cultures and senior leaders are implicated in misconduct only 15 percent of the time in the strong culture companies. Broader, pervasive misconduct as opposed to one-time-only misdeeds involving a single person also is far lower when culture is strong.

IN LARGE COMPANIES WITH STRONG CULTURES, THERE ARE FEWER MANAGEMENT LEVEL EMPLOYEES INVOLVED IN MISCONDUCT

WEAK CULTURE: Senior Leader 23%, Middle Manager 25%, First-Line Supervisor 23%, Non-management 28%

STRONG CULTURE: Senior Leader 15%, Middle Manager 18%, First-Line Supervisor 20%, Non-management 47%

- ■ Senior Leader
- ■ Middle Manager
- ■ First-Line Supervisor
- ■ Non-management

In conventional wisdom, large organizations are sometimes considered too dispersed and unwieldy to be managed effectively. Culture is sometimes said to reflect local circumstances and traditions, so that each office or work location in a large organization takes on an identity of its own. But our data show that even very large companies can successfully manage their ethics cultures,
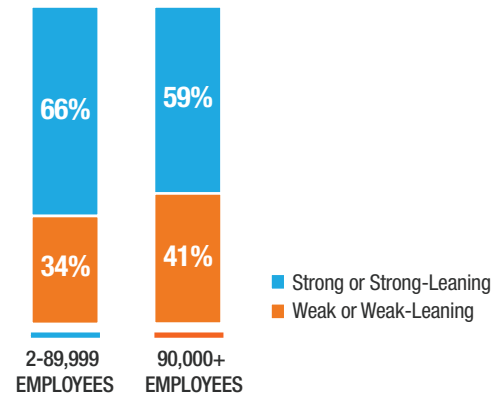
creating and maintaining companywide standards of conduct.

Big companies can, in fact, set high ethical standards and enforce them. Well implemented ethics and compliance programs make a difference, often a big difference. And, it is possible to build strong cultures in even the largest companies. Large companies that commit to ethical performance can cut misconduct, increase employee reporting of wrongdoing that does occur, and also trim both pressure and retaliation to a bare minimum.

Strong Ethics Cultures Less Likely in Large Companies

Perhaps the most striking difference between large companies and smaller ones is related to the strength of ethics cultures. Large companies are more likely to have a weaker ethics culture compared to small companies.

ETHICS CULTURES WEAKER IN LARGER COMPANIES

2-89,999 EMPLOYEES: Strong or Strong-Leaning 66%, Weak or Weak-Leaning 34%

90,000+ EMPLOYEES: Strong or Strong-Leaning 59%, Weak or Weak-Leaning 41%

- ■ Strong or Strong-Leaning
- ■ Weak or Weak-Leaning

Past ERC research has shown that strength of ethics cultures is the key driver of ethics outcomes. The difference found in the strength of ethics culture is likely the cause of the differing rates of observed misconduct. Fifty-one percent of employees in large companies (90,000 or more employees) observed misconduct, where 41% of employees in smaller companies (under 90,000 employees) observed misconduct.[1] Large companies can control their own ethical destiny, which will improve their ethics outcomes.

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1. See page 5.

SNAPSHOT OF ETHICS IN LARGE COMPANIES

KEY ETHICS OUTCOMES	IN COMPANIES WITH 90K + EMPLOYEES
Felt pressure to compromise standards	10%
Observed misconduct in the previous 12 months	51%
Reported misconduct when observed	66%
Reporters who experienced retaliation	15%

MOST COMMON FORMS OF MISCONDUCT IN COMPANIES WITH 90K+ EMPLOYEES	PERCENT OF EMPLOYEES WHO OBSERVED IN PREVIOUS 12 MONTHS
Lying to employees	25%
Abusive behavior or behavior that creates a hostile work environment	20%
Conflicts of interest	16%
Discrimination	16%
Violating company policies related to Internet use	16%
Lying to outside stakeholders	16%

FORMS OF MISCONDUCT WITH LOWEST REPORTING RATES	PERCENTAGE OF OBSERVERS WHO FAILED TO REPORT
Violating company policies related to Internet use	70%
Making improper political contributions to officials or organizations	61%
Falsifying invoices, books, and/or records	60%
Falsifying and/or manipulating financial reporting information	60%
Discrimination	60%
Breaching employee privacy	59%
Lying to employees	58%
Lying to outside stakeholders	58%

MOST COMMON TYPES OF RETALIATION	PERCENTAGE OF RETALIATION VICTIMS WHO EXPERIENCED THE NOTED TYPE
Supervisor intentionally ignored or began treating employee differently	69%
Verbally abused by supervisor or someone else in management	55%
Other employees intentionally ignored or began treating differently	49%
Supervisor or management excluded employee from decisions and work activity	48%
Not given promotions or raises	48%

DOES COMPANY SIZE MATTER?
How Company Size Does – and Does Not – Predict Ethical Health

A quick comparison of key outcomes reveals a more nuanced picture of the ways that company size does and does not make a difference.

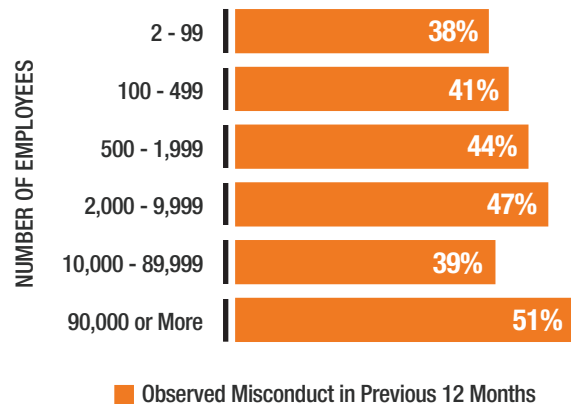|	Under 90K employees	90K + employees
Felt pressure to compromise standards	9%	10%
Observed misconduct in the previous 12 months	41%	51%
Reported misconduct when observed	63%	66%
Reporters who experienced retaliation	22%	15%

Items in RED are statistically worse. Items in GREEN are statistically better.

Observed Misconduct

Although observed misconduct is more common in the largest companies, the reality of misconduct is more complicated than it might initially seem.

For example, the misconduct rate in the largest companies is higher than all smaller companies as a whole. But, when comparisons are made using narrower categories for company size, the largest companies (i.e., those with 90,000 or more employees) are statistically equivalent to companies with 2,000 to 9,999 employees. The lowest misconduct rates actually occur in companies with fewer than 500 employees and those with 10,000-89,999 employees. Simply put, more employees does not necessarily mean more misconduct.

MISCONDUCT VARIES ALONG WITH COMPANY SIZE

NUMBER OF EMPLOYEES

2 - 99	38%
100 - 499	41%
500 - 1,999	44%
2,000 - 9,999	47%
10,000 - 89,999	39%
90,000 or More	51%

■ Observed Misconduct in Previous 12 Months

5

Investigation into specific forms of misconduct also reveals a more complicated picture. The top five forms were the same in companies with 90,000 or more employees as in smaller (i.e., those with fewer than 90,000 employees) companies. And the frequency of incidents observed (i.e., Did it happen once, multiple times, or as an ongoing pattern?) was statistically equivalent regardless of company size.

Despite these similarities, some important differences do exist. Of the 26 kinds of misconduct in the survey, 15 were significantly more common in the largest companies (i.e., those with 90,000 or more employees) compared to smaller ones (i.e., those with fewer than 90,000 employees). For example, the rate of fraud, waste, and abuse in large companies was 41 percent, compared to 34 percent in smaller companies.

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The rate of fraud, waste, and abuse in large companies was 41 percent, compared to 34 percent in smaller companies.

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Reporting of Observed Misconduct

Reporting patterns are very consistent, regardless of company size. Rates do not vary based on company size. Even when companies are compared by six narrower size categories, rates are statistically equivalent. Furthermore, reporting rates for 25 of 26[2] forms of misconduct are the same. And, regardless of company size, reporting locations (i.e., who employees choose to tell) are nearly identical.

Retaliation Against Whistleblowers

Overall, retaliation was less common in large companies (i.e., those with 90,000 or more employees) than in smaller ones (i.e., those with fewer than 90,000 employees). However, the types of retaliation experienced do not differ significantly with company size. In fact, the five most common types of retaliation were the same in smaller and larger companies.

WHERE EMPLOYEES REPORT IN COMPANIES WITH LESS THAN 90K EMPLOYEES
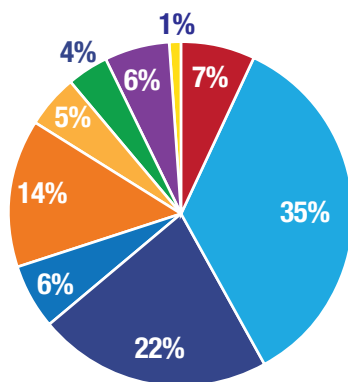
WHERE EMPLOYEES REPORT IN COMPANIES WITH 90K OR MORE EMPLOYEES
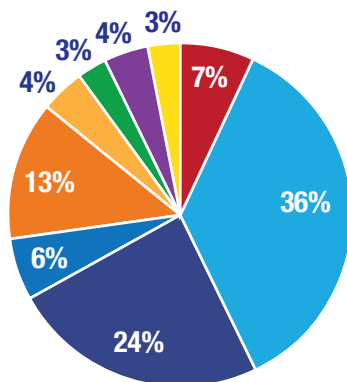
Legend: ■ Hotline ■ Supervisor ■ Higher Management ■ Ethics Officer ■ HR ■ Legal ■ Government/Regulatory Authority ■ Outside Non Government ■ Other

2. The single exception is discrimination, in which the reporting rate is 48 percent in companies with fewer than 90,000 employees and 40 percent in larger companies.

Which Matters More: Programs or Culture?

Both effective ethics and compliance programs and strong ethics cultures are linked to greatly improved outcomes. But which matters more? A straight comparison of the two factors reveals that ethics culture is linked to more profound reductions in rates of pressure to compromise standards and observed misconduct. Pressure is reduced by 36 ppts in a strong culture compared to a weak one; while it is reduced by only 20 ppts in companies with an effective versus an insufficient or ineffective program.

Program effectiveness coincides with vastly improved reporting rates and decreased retaliation against whistleblowers. Companies with effective programs see a 55 ppt increase in reporting compared to companies with insufficient or ineffective programs; those companies see only an 18 ppt increase in reporting.

Both effective ethics and compliance programs and strong ethics cultures make a difference. Effective programs and strong cultures are not independent of one another. Rather, they reinforce each other, working together to improve the workplace environment. Choosing one over the other is a false dichotomy.

	WHICH MATTERS MORE: PROGRAMS OR CULTURE?					
	Indicators of Program Effectiveness			Strength of Ethics Culture		
Key Ethics Outcomes	None or Don't Know to all	All 6	PPT Improvement[3] Related to Effectiveness of E&C Program	Weak[4]	Strong	PPT Improvement Related to Strength of Ethics Culture
Felt pressure to compromise standards	23%	3%	-20%	42%	6%	-36%
Observed misconduct in the previous 12 months	62%	33%	-29%	89%	42%	-47%
Reported misconduct when observed	32%	87%	55%	55%	73%	18%
Reporters who experienced retaliation	59%	4%	-56%	58%	8%	-50%

3. PPT improvements are calculated based on unrounded percentages. PPT = percentage points, or the difference between the two results. In these cases regarding reporting of personally identified misconduct and ERC listed misconduct, the 13 ppt improvements Overall is arrived at by subtracting 52 from 65.

4. NOTE: Comparisons are based on a three-tiered measure of culture.

Past ERC research[5] has proven that ethics and compliance programs help build strong ethics cultures. This seems to be particularly true in large companies, as demonstrated by data from the 2011 National Business Ethics Survey which measured program comprehensiveness and program effectiveness compared to strength of ethics cultures. Among larger companies (100,000 or more employees), only one in five (20 percent) is able to have a strong ethics culture without a comprehensive, effective program at its foundation. In smaller companies (i.e., those with fewer than 100,000 employees), the situations are somewhat better – nearly one out of every three companies (32 percent) with insufficient or ineffective programs has a strong ethics culture. And, although both size companies benefit when a comprehensive, effective ethics and compliance program is in place, large companies benefit even more. In them, 93 percent have strong or strong leaning ethics cultures compared to 90 percent of small companies having such cultures. **Companies, especially large companies, that want to see positive ethics outcomes should focus on comprehensive, effective programs AND the strong ethics cultures they build.**

2011 NBES DATA DEMONSTRATE THAT ETHICS PROGRAMS ARE MORE CRITICAL TO CULTURE-BUILDING IN LARGE COMPANIES

LESS THAN 100,000 EMPLOYEES		
Insufficient or Ineffective Program	32%	
Comprehensive & Effective Program		90%

100,000 OR MORE EMPLOYEES		
Insufficient or Ineffective Program	20%	
Comprehensive & Effective Program		93%

■ Strong or Strong Leaning Ethics Culture
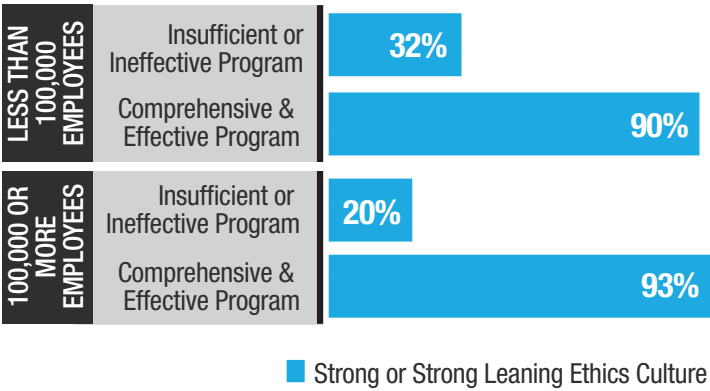
When a comprehensive, effective ethics and compliance program is in place, strong ethics culture are the norm--in companies of all sizes.

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5. Ethics Resource Center (2012). *Ethics Resource Center's National Business Ethics Survey.* Arlington, VA: Ethics Resource Center.

Implications of the Findings:
What Should You & Your Company Do?

ERC's investigation of the state of ethics in America's largest companies reveals the profound difference that effective ethics and compliance programs and strong ethics cultures can make.

To ensure E & C program effectiveness:

■ **Assess the effectiveness of your program.** Investigate whether your program is a vital, living part of your organization. Determine areas of strength to build on as well as potential trouble spots. Explore whether your program is effective on multiple levels: in different divisions, various regions, across departments and functions, and at all employee levels.

■ **Look critically at reward and recognition systems as well as the advancement track for employees.** Ensure that ethical conduct is praised and celebrated and that ethical conduct is a decisive factor in decisions about promotions and bonuses.

To promote a strong ethics culture:

■ **Model from the highest levels.** Starting from the top leaders at all levels should intentionally demonstrate transparency. They also should show openness to new ideas, constructive criticism, and thoughtful dissent.

■ **Make ethical leadership a component of management training.** Evaluate supervisors on their awareness of and appreciation for ethical conduct by their reports.

■ **Invest in training programs and ethics advice resources that are pragmatic, approachable, and accessible.** When developing training, ask employees about the ethics challenges they face in their jobs and equip them with the knowledge and skills they need to address them. Make sure that your ethics advice resources include several options (in person; via phone, email, or online) and take advantage of effective internal communications vehicles, such as your internal corporate social network.

Program effectiveness, ethics culture strength, and ethics outcomes can vary by organizational units, locations, employee functions, and other geographical demographics. Larger organizations should measure the internal ethics environment to ascertain these differences. Based on those findings, larger companies should develop targeted responses, apply transferable best practices from successful units to other units and develop unit-specific remediation strategies to help create a uniformly ethical work environment.

All data used for this report was collected as part of ERC's 2013 National Business Ethics Survey® (NBES®), which captures the views of private sector workers in the United States. It provides a comprehensive look at trends in workplace ethics and compliance and also offers the most exacting longitudinal cross-sectional data about conduct at work.

The 2013 NBES reflects responses from 6,420 private sector workers. Participants were 18 years of age or older; currently employed at least 20 hours per week for their primary employer; and working for a company that employs at least two people. All participants were assured that their individual responses to survey questions would be confidential. Participants were randomly selected to attain a representative national distribution. About one-quarter of survey participants were interviewed by telephone. Of these, approximately 33 percent were interviewed over landlines and 67 percent over cellphones. The remaining three-quarters of the survey population participated through an online survey (using online panels and communities). The proportion of the cellphone group to the landline group in the sample was weighted to a 40/60 ratio.[1] The proportion of telephone respondents to online respondents was weighted to be equal.[2]

In addition, we oversampled for employees of companies with 90,000 or more employees and interviewed about 1,600 workers from these large companies. Large-company data presented in this report have been drawn from this oversampled population. NBES data, overall, have been weighted to correct for this oversampling.

The survey opened September 30, 2013, and closed November 15, 2013. Survey questions and sampling methodology were established by ERC; data collection was managed by Survey Sampling International (SSI). The sampling error of the findings presented in this report is +/- 1.2 percent at the 95 percent confidence level. Data were weighted by age, gender, and education. Data were additionally weighted by phone type (cell/landline), survey mode (telephone/online), and organization size as described above.

To request a detailed explanation of methodology and the methodological limitations of this report and demographic information on survey participants, please email the Ethics Research Center at ethics@ethics.org.

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1. The cell 40 / landline 60 ratio is an estimation of the proportion of working individuals living in households with cell-only service versus households with landlines.

2. The equal-weight strategy was implemented because survey results from the two groups tended to differ, and it matched the methodology used in 2011. It is part of an ongoing transition from a landline telephone-only survey to a mixed telephone/online survey, and eventually to an online-only survey. The weighting equalized the influence of each group and provided comparability to the 2011 iteration of the study.

ETHICS & COMPLIANCE INITIATIVE

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