

Chapter 2

The Ethical Challenge: An Italian Way Through Organisational Models and Theories

2.1 Ethics and the Responsibility of Legal Persons in Italy: The Legislative Decree n. 231/2001

Corruption and fraud against public administration in Italy are endemic, as reported in the Transparency International rankings: in 2014, Italy is ranked 69 (69 in 2013 and 72 in 2012) out of the 177 observed countries, on a corruption perception index, which measures the perceived levels of public sector corruption. The Italian Court of Audit has pointed out that the total direct cost of corruption amounts to 60 billion euro each year (equivalent to approximately 4 % of GDP). Since 2012, the president of the Court of Audit has reiterated his concerns every year as to the impact of corruption on the national economy. This situation does not improve if we consider other sources such as Greco—Group of States against Corruption Commission—who in the report entitled “Joint First and Second Evaluation Round—Evaluation Report on Italy” in 2009 says “*despite the clear commitment of judges and prosecutors to deal effectively with corruption instances, corruption is perceived in Italy as a pervasive and systemic phenomenon, with numerous areas of activity (in particular, urban planning, public procurement and the health sector) and territories being affected. While a considerable arsenal of legislation has been passed, more needs to be done to articulate an effective preventive policy in this area*”. Hence, the invitation to Italy to react to this situation with a strong push towards prevention “*there is still room for further improvement as regards transparency and ethics of public administration*”, and improved transparency and ethics in public management, even though “*This would require a long term approach and sustained political commitment; combating corruption has to become a matter of culture and not only rules*” (Council of Europe 2009).

Most recently in Annex 1 to the EU Anti-Corruption Report of the 3rd of February 2014, the European Commission said “*however, despite considerable efforts by the Court of Audit, law enforcement bodies, prosecution services and the judiciary, corruption remains a serious challenge in Italy. [...] Overall, further*

efforts need to be made to ensure effective implementation and monitoring of the anti-corruption legal framework, including the legislative decrees, to secure a sustainable impact on the ground”.

It was in reaction to this situation that Legislative Decree no. 231 was issued in 2001 to implement article 11 of Enabling Act no. 300 of 29 September 2000, whereby the Government was to define a penalties system for the administrative liability of bodies (Italian Government 2001) in compliance with the obligations set out by a number of important international acts: the Convention on the protection of the European Communities’ financial interests of 26 July 1995, the Convention on the fight against corruption involving officials of the European Communities or officials of Member States of the European Union approved in Brussels on 26 May 1997 and the OECD Convention of 17 September 1997 on the fight against corruption involving foreign public officials in international economic transactions. In particular, this latter states (OECD 1997)

The Parties,

Considering that bribery is a widespread phenomenon in international business transactions, including trade and investment, which raises serious moral and political concerns, undermines good governance and economic development and distorts international competitive conditions;

Considering that all countries share a responsibility to combat bribery in international business transactions;

shall take such measures as may be necessary to establish that it is a criminal offence under its law for any person intentionally to offer, promise or give any undue pecuniary or other advantage, whether directly or through intermediaries, to a foreign public official, for that official or for a third party, in order that the official act or refrain from acting in relation to the performance of official duties, in order to obtain or retain business or other improper advantage in the conduct of international business.

Article 2 establishes the fundamental principle of the “Responsibility of Legal Persons”

Each Party shall take such measures as may be necessary, in accordance with its legal principles, to establish the liability of legal persons for the bribery of a foreign public official.

and Article 3 establishes the corresponding sanctions

In the event that, under the legal system of a Party, criminal responsibility is not applicable to legal persons, that Party shall ensure that legal persons shall be subject to effective, proportionate and dissuasive non-criminal sanctions, including monetary sanctions, for bribery of foreign public officials.

This has led to a change in the Italian regulatory system: indeed, before Legislative Decree no. 231/2001, a company’s responsibility for offences committed in its interest or to its advantage by directors and/or employees was limited solely to civil obligation, i.e. payment of the fines and penalties inflicted and only in the event of insolvency of the offender, pursuant to article 197 of the Italian Criminal Code, and to the obligation of restitution and damages pursuant to article 185 of the Italian Criminal Code.

The Decree provides a new form of liability, which the legislator describes as “administrative”, that is independent from the liability of the individual who has actually committed the crime. Indeed, according to the provisions of Article 8, the organisation may be held liable even if the individual who has committed the crime cannot be charged or identified. Whence it follows that the organisation is not liable if the individual who committed the crime acted solely in his/her own interest or in the interests of third parties, or in the event that the organisation may not be charged with “corporate criminal liability”. More in detail, Article 5 of the Decree establishes that the organisation is responsible for crimes committed in its interest or to its gain by individuals who are representatives, directors or managers of the company or of one of its organisational unit that has financial and functional independence, or by individuals who are responsible for managing or controlling the company (individuals in apical positions) and by individuals who are managed or supervised by an individual in an apical position (individuals under the command of others).

Article 9 of the Decree sets out the following administrative penalties: fines whose maximum sanction is 1.5 million euro, disqualification, seizure and publication of the decision. In particular, disqualification can be the following: disqualification from exercising company activity up to 24 months; suspension or cancellation of authorisations, licences or concessions needed to commit the unlawful act; prohibition on entering into contracts with the public administration, unless done so in order to obtain a public service; exclusion from benefits, loans, contributions or subsidies and possible cancellation of those already granted; and prohibition on publicising goods or services. Hence, the assessment of liability may entail the application of severe penalties that could compromise the existence of the body.

It is clear that the Decree covers a large range of felonies that can be committed by persons in the interest or to the advantage of the company. In effect, Legislative Decree n. 231 is substantially an open normative that is subject to continuous integration and updating according to the type of responsibility periodically revised. For example, in 2001 the Decree dealt with “white collar” crime”, in 2011 it was integrated to include environmental crimes and in 2012 employment crimes. Currently, the number of felonies which imply administrative responsibility is more than 160 (Fig. 2.1).

The crimes contemplated under the Decree which directly concern the activity performed by a company involve, among others, the following:

- Article 24—fraud committed against the Italian state or another state institution in order to receive public funds and electronic fraud against the Italian state or another state institution
- Article 24 bis—computer crime and unlawful treatment of data (Italian Law 48/08)
- Article 25—extortion and corruption
- Article 25 bis—felonies against industry and commerce

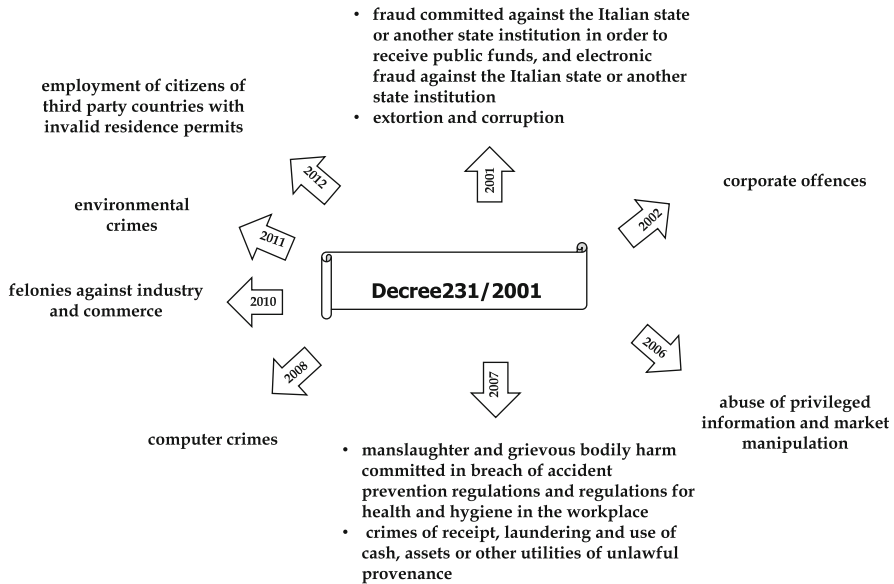


Fig. 2.1 Crimes contemplated under the decree

- Article 25 ter—corporate offences such as false reporting to the prejudice of shareholders or creditors, false statements in a prospectus, false reports or notices drawn up by the auditing company, sham formation of capital, unlawful restitution of contribution of capital, illegal distribution of profits and reserves, operations injurious to creditors
- Article 25 sexies—abuse of privileged information and market manipulation
- Article 25 septies—manslaughter and grievous bodily harm committed in breach of accident prevention regulations and regulations for health and hygiene in the workplace (Italian Legislative Decree 81/08)
- Article 25 octies—crimes of receipt, laundering and use of cash, assets or other utilities of unlawful provenance (Italian Legislative Decree 231/07)
- Article 25 novies—felonies regarding breach of copyright
- Article 25 decies—inducements not to make statements or to make false statements to the courts
- Article 25 undecies—environmental crimes
- Article 25 duodecies—employment of citizens of third party countries with invalid residence permits

2.2 The Company's Responsibility and Organisational Models

What is clear from the above summary is that a company's objective liability is irrespective of the effective guiltiness of the company, hence the need to better define this kind of responsibility, especially in terms of organisational responsibility. In effect, under articles 6 and 7 of the Decree, the company body may be exempted from liability if it can prove it has adopted and effectively implemented an organisational, management and control model designed to prevent the said offences. In fact, under paragraph 2 of article 6 and paragraph 4 of article 7 of the Decree, the lawmaker establishes that this organisational model must meet the following requirements:

- (a) The Board of Directors adopted and efficiently enacted, prior to commission of the act, organisational and management models which are capable of preventing offences of the type occurring.
- (b) The task of overseeing such operations, compliance with the models and seeing to updating of the same has been delegated to a Supervisory unit vested with powers to act on its own initiative and conduct monitoring.
- (c) The persons committed the offence by fraudulently circumventing the organisational and management models.
- (d) There has been no omission or insufficient oversight on the part of the Supervisory unit referred to in subparagraph (b).

With regard to the extension of delegated powers and the risk of committing offences, the models referred above must fulfil the following requirements:

- (a) Identify the activities in relation to which offences may be committed.
- (b) Provide specific direct protocols and schedule training and implementation of decisions by the body regarding offences to be prevented.
- (c) Identify procedures for managing financial resources which are fit to prevent the commission of offences.
- (d) Provide obligations to disclose information to the organisation tasked with overseeing the working of and compliance with the models.
- (e) Introduce a new disciplinary system to punish noncompliance with the measures set out in the model.

At this point, it's important to specify that the Decree does not require the adoption of an organisational model or of a supervisory unit. No fines are applied in the case of no adoption; however, it does expose the company to major risk. Therefore, the organisational model, despite the fact that it is voluntary, becomes a fundamental *conditio sine qua non* if the company wants to take advantage of the form of exemption from liability, outlined in Article 6 (Fig. 2.2).

That said, problems arise from the vague definition of both the organisational model and supervisory unit. The Decree does not explain the managerial and organisational models in detail; the norm requires only that:

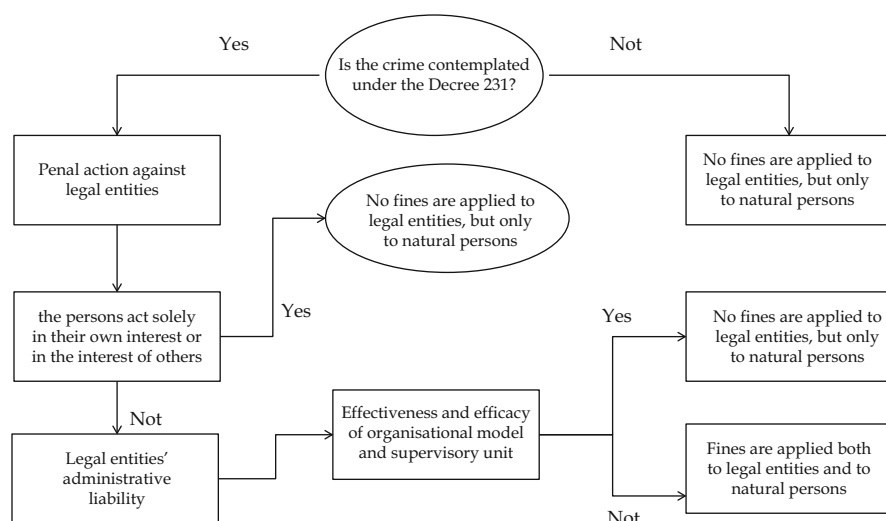


Fig. 2.2 Administrative liability and legal entities

- The control system be planned in order to identify, measure and adequately monitor all the risks related to the different operational areas.
- Control processes and activities are established at each operational level.
- A reliable information system is insured that is able to refer any anomalies that emerge during the control process instantly.
- Each managerial fact is registered in adequate detail.
- A supervisory unit that has been vested with autonomous powers of initiative and control is established, which is able to supervise the functioning and enforcement of organisation, management and control models suitable for preventing the perpetration of the criminal offences specified in the Decree.

The same vagueness also occurs in OECD documents such as “Annex II of the recommendation of the Council for further combating bribery of foreign public officials in international business transactions adopted by the Council on 26 November 2009” (OECD 2009):

Effective internal controls, ethics and compliance programmes or measures for preventing and detecting foreign bribery should be developed on the basis of a risk assessment addressing the individual circumstances of a company, in particular the foreign bribery risks facing the company (such as its geographical and industrial sector of operation). Such circumstances and risks should be regularly monitored, re-assessed and adapted as necessary to ensure the continued effectiveness of the company’s internal controls, ethics and compliance programme or measures; ethics and compliance programmes or measures designed to prevent and detect foreign bribery, applicable to all directors, officers and employees and applicable to all entities over which a company has effective control and to all third parties such as agents and other intermediaries, consultants, representatives, distributors, contractors and suppliers, consortia and joint venture partners; a system of financial and accounting procedures, including a system of internal controls, reasonably designed to ensure the maintenance of fair and accurate books, records and accounts, to

ensure that they cannot be used for the purpose of foreign bribery or hiding such bribery; measures designed to ensure periodic communication, and documented training for all levels of the company, on the company's ethics and compliance programmes or measures regarding foreign bribery, as well as, where appropriate, for subsidiaries;

The general features of the law have highlighted the following critical aspects in the enforcement of the new liability regime: the first aspect is related to the effective interpretation and understanding of the guiding principles of the regulation. The main problem is to identify the boundaries and the range of management models that can be used as a means of deterring offences and granting liability exemption to the entities. In other words, when analysing the Decree it becomes evident that, despite the effort made by the legislator to clarify and make its measures easily enforceable, the exact specification of the nature and the suitable level of precision in the adoption of the organisational, management and control models and procedures is a complex and wide subject. A second important consideration concerns the identification of the supervisory unit. Here, the focus is on the trade-off between the nature of the agent in charge of the control and the quality and operability of this control. It may appear appropriate and more useful, in order to achieve a better degree of precision, to give a qualified outsourcing body the responsibility of controlling the adoption and compliance of the organisational models. This is in order to guarantee the organisation's effective independence from possible constraints that may be created by a hierarchy. While a supervisory unit composed of company managers and officers would mean a cost reduction it also means a lack of autonomy and independence of judgement.

Therefore, the presumed calculation of costs and benefits, prior to the adoption of the models, has to take into account the probability that some offences, e.g. of minor consistency or of difficult detection, may remain unpunished. We have already seen that the adoption of models, which enforce the necessary measures to avoid expensive sanctions, is not compulsory. This implies that the firm faces a dilemma about whether to choose the adoption of sophisticated management models with an independent supervisory unit or conversely to adopt a strategy of cost saving, based on the probability that the offence may be disclosed and sanctioned *ex post*.

If we call on organisational theories to help us, we face the lack of an unequivocal understanding of organisational models, as described in Chap. 1. If we embrace the contingency theory, we will plan an organisational model according to "contingency factors" such as technology, size, environment, etc.; if we adopt the classic theories, we will look for and follow an ideal "Do it Yourself" manual, without any distinctions being made as to the company's size, technology or industry; in adopting the new institutionalism theory, we will look for organisational characteristics such as "rites and ceremonies" common to all types of companies; with transaction cost theory, our interest will focus on how and what part of the organisational model should be managed inside and how and what outside the company and finally, if we apply population ecology theories, we will look for the features of organisational models which allow companies to survive

competition better, or to gain more resources in the case of resource dependence theory.

Given this uncertainty, the support and interpretation given to the “concept of the organisational model” by trade associations which have, in recent years, provided specific guidelines and useful hints on organisational model design and implementation to several industries (insurance, banking, pharmaceutical, etc.) become important. In March 2014, for example, Confindustria (the Italian national trade association) issued new guidelines which define some key principles of organisational models:

- Segregation of activities: there must be segregation of activities between those who execute, those who control and those who authorise the transactions
- Existence of formalised norms and rules: there must be company directives that can provide at least general reference principles for regulating activities, responsibilities and controls
- Existence of delegations and powers-of-attorney: there must be formalised rules for exercising delegations and powers-of-attorney
- Traceability: the individuals, functions/organisational units concerned and/or the information systems used must ensure the identification and reconstruction of the sources, the informative elements and the controls performed that support the training and the implementation of company decisions and the procedure for managing financial resources
- Organisational models must be formalised and made explicit through organisation charts and job descriptions, clear task and responsibilities assignment, with some specific principles of control such as segregation of duties and combined method for signature
- Assignment of decisional powers and delegations which fits the organisation levels
- Accounting transparency grounded on the use of true, accurate and complete information which form the basis for the entries in the books of accounts. Operational events must be properly and timely registered in the books of accounts
- For each transaction, the proper supporting evidence has to be maintained in order to allow
 - Easy and punctual accounting entries
 - Identification of different levels of responsibility, as well as of task distribution and segregation
 - Accurate representation of the transaction so as to avoid the probability of any material or interpretative error
- Wide dissemination of the principles and contents of the organisational model among all the employees through specific communication and training courses
- A supervisory unit with autonomy and independence guaranteed by the position recognised to it within the organisational structure of the company and by the

necessary requisites of independence, good reputation and professionalism of its members

Another important source of clarification is jurisprudence, and in particular it's worth analysing the Decree established by the Tribunal of Milan on November 9, 2014 which outlines ten key requirements for an optimal organisational model pursuant to Legislative Decree 231:

- (1) The identification of corporate activities which may entail the risk of committing the offences provided for by Legislative Decree no. 231 of 2001 as a result of corporate process analysis, and not a mere description and repetition of that established by the law
- (2) Members of the supervisory unit must have specific competencies in control, audit, risk analysis and inspection
- (3) Absence of judgment for the members of supervisory unit, even if it is not yet final, or application of the sanction on request (the so-called plea-bargaining), in Italy or abroad, for the violations relevant to the administrative liability of legal entities
- (4) Principles and contents of Legislative Decree no. 231 of 2001 and of organisational model must be explained in training courses. Attendance at the courses is mandatory. The structure of the training courses could be either general or more detailed depending on the specific area of risk
- (5) The supervisory unit must control the quality of the compulsory training courses
- (6) A disciplinary system, with definition of sanctions appropriate for the violation committed and applicable in case of breach of the organisational model, extendable to executives and directors
- (7) Specific control standards, which contain special provisions aimed at governing the typical aspects of sensitive activities and which must be included in corporate reference procedures
- (8) A control system based on several types of control, both standard and random inspection
- (9) A set of procedures which ensures any remarks and information concerning a possible violation or any request to violate the code of ethics and the law is immediately reported to their superiors and the supervisory unit
- (10) Specific protocols and procedures truly embedded into daily behaviour

Finally, it's useful to mention the best practices suggested by consulting companies and senior experts (Table 2.1). According to this sector, the organisational model is composed of the following elements:

- A code of ethics, which promotes values such as compliance with the law, regulations, statutory provisions, self-regulatory codes, ethical integrity and fairness. Business and corporate activities have to be carried out in a transparent, honest and fair way, in good faith and in full compliance with competition protection rules. Compliance with the code by directors, management and

Table 2.1 Concept of the organisational model

Trade associations' guidelines	Jurisprudence	Best practices
✓ Specific communication and training courses	✓ Detailed corporate process analysis	✓ A code of ethics
✓ A supervisory unit with autonomy and independence	✓ Members of the supervisory unit with specific competencies	✓ An organisational model—general part
✓ Existence of formalised procedures, job descriptions, organisational chart and delegation of power	✓ Specific protocols and procedures	✓ An organisational model—special parts
✓ Segregation of activities	✓ Specific control systems and standards	✓ A documented company map of areas at risk
✓ Traceability, accounting transparency and accurate representation	✓ A disciplinary system	✓ An internal control system
	✓ Compulsory training courses	✓ A specific disciplinary system

employees, each within their own functions and responsibilities, is of paramount importance

- An organisational model—general part—illustrates the criteria and principles of the Decree, the governance model and the principles of the internal control system. It also describes the component parts of the model, including the role of the supervisory unit appointed to oversee its functioning, compliance to it and keeping it up to date
- An organisational model—special parts—provides a description of the types of crime contemplated by the Decree. Each special part contains a legal analysis of the individual crimes mentioned in the Decree and the general principles of conduct which should inspire conduct in all the areas potentially at risk of crime for each special part. For each area at risk, the company functions involved are indicated, as well as the “sensitive activities”, the specific crimes theoretically possible, how they could be committed or the forms of conduct leading to their commission, preventive controls and the duties of the supervisory unit in this regard
- A specific disciplinary system that will sanction noncompliance with the measures indicated in the model
- A documented company map of areas at risk, i.e. identification of the company areas/sectors in which the commission of the prejudicial deeds indicated in the Decree is theoretically possible, and analysis of how the crimes might be committed and the history of the entity
- An internal control system reasonably capable of preventing or reducing the risk of commission of crimes through the adoption of suitable procedures and protocols

2.3 Compliance and Organisational Models: Rhetorical or Technical Requirement?

As argued in the previous paragraph, to prevent corruption through the establishment of ethical standards, it's important to focus our attention not just on the fines and responsibilities applicable in the case of non compliance but also on the organisational model, so as to increase transparency, accountability and control, especially for companies that receive public funds. It is clear that there is a strong risk of creating a compliance system that is merely formal and paper-based and that has no real impact on organisational behaviour, even more so if compliance is required by law.

Under these assumptions, a question is raised as to how rhetorical or real compliance pursuant to Decree 231 is. Zbaracki (1998) suggests that this kind of compliance—and this is true for other practices such as total quality management too—implies a technical intervention that can become both ambiguous and sometimes dubious. It is almost as if there are two versions of compliance: a technical version, which incorporates some fairly well-defined organisational interventions and control procedures, and a second more rhetorical version that seems to carry a sort of rhetorical excess (Hackman and Wageman 1995) and ambiguous terms where organisational implications and improvements are unclear. This dichotomy raises some crucial questions: does compliance under Decree 231 lead to a change in organisational model? Does the supervisory unit perform an effective control on preventing risks and felonies? To what extent do the procedures become real executive behaviour?

Distinguishing between “a technical organisational model” and a “rhetorical organisational model” recalls a long-standing claim of institutional theory (DiMaggio and Powell 1991) as outlined in Chap. 1, which describes a process whereby the symbolic value of something like the organisational model ultimately supplants its technical value. Using an organisational model pursuant to Decree 231 may provide an organisation with little technical benefit, but the claim of using it confers legitimacy on the organisation (Westphal et al. 1997). Consequently, managers will use the “rhetorical 231” largely in a formal and symbolic way to gain legitimacy without necessarily affecting activities at the technical core of the organisation (Meyer and Rowan 1977). Edelman (1992) argues that this poses a dilemma for organisations: they must appear attentive to the law in order to gain legitimacy and public resources and, at the same time, seek to minimise the law's constraints on traditional managerial prerogatives. Hence, organisations respond to this dilemma by creating symbolic structures, which serve as visible efforts to comply with the law. Edelman points out that because the normative value of these structures does not depend on their effectiveness, they do not guarantee substantive change in organisational behaviour.

In effect, our case is a special example of organisational form which can be observed not only as “coercive isomorphism” due to the application of a law but also as “normative isomorphism” due to guidelines and procedures issued by trade

associations and other stakeholders, as well as “mimetic isomorphism” since its application is very specific to industries where organisations work closely together.

A final consideration to be made is the application of the framework of analysis to the “law and society” school. When addressing the impact of legal rules on organisational behaviour, institutional theorists generally assume that organisations know what the law is. Law and society research, however, suggests that this superficially plausible assumption may be seriously flawed, and they point to at least three distinct characteristics of law that render it uncertain rather than determinate: legal ignorance, legal pluralism and legal ambiguity. As regards legal ignorance, legal systems have no automatic mechanism for disseminating information about law, therefore people learn lessons about the law from the media, the professions, the education system and first-hand experience, and this leads to inaccurate, superficial and incomplete knowledge. As concerns legal pluralism, formal rules are transformed by the local regulators (e.g. Italian Regions, jurisprudence, etc.), and so they may differ dramatically from one local community to another. Finally, the law is ambiguous as a result of a process where the law is actually a welter of conflicting principles, imperfect analogies and ambiguous generalities, where lawyers, judges, enforcers and target populations negotiate the meaning of law in each application, seeking workable consensus rather than logical certainty. As noted above, institutional processes through trade association guidelines and best practices about the interpretation of organisational models pursuant to Decree 231 often generate agreements about the contents of legal mandates and about the standards of legal interpretation; nonetheless, a shared convention is not really the same thing as an objective meaning, and at some level, every application of law remains fundamentally an exercise in social creativity. Contrary to the casual assertions of institutional theorists, it is simply untrue that organisations can only be in compliance or not in compliance with legislative Decree 231 (Edelman et al. 1991). Given these observations, the law may best be conceptualised not as an objective external constraint but rather as a source of uncertainty in organisational life: courts, enforcement agencies, lawyers and target populations themselves can all transform the meaning of the law and the definition of compliance.

2.4 From Compliance to Business Ethics

As we have seen in the previous paragraph, Decree 231 and the general laws that regulate organisational behaviour are quite vague and set out broad and ambiguous principles rather than dictating specific behaviours (Diver 1980; Hawkins 1984; Edelman 1992). Hence, organisations have wide latitude in determining how, if at all, to comply. In this context, the creation of symbolic structures is especially attractive: an organisation can point to structural change as evidence of its compliance, without necessarily creating significant change in behaviour, even though the creation of symbolic structures is only the first stage of organisational response to

law. The literature on regulation and on organisational behaviour tends to emphasise the capacity of organisations to resist compliance with law. This is especially true for studies of regulatory agencies, which overwhelmingly emphasise noncompliance (Katz 1977; Wirt 1970; Blumrosen 1965), show how organisational structure encourages inattention to legal requirements (Stone 1975) and show how the internal normative environment of organisations often encourages individuals to place organisational goals over legal goals when the two conflict (Vaughan 1983).

Maybe compliance should be understood as a social and political process that evolves over time rather than as a discrete event or non-event, or the existence or non-existence of compliance. And to be effective, a process of compliance must start with ethics and organisational culture.

Edwards (2003) and Edwards and Wolfe (2004) define compliance as the adherence by the regulated to rules and regulations laid down by regulators, uniting a rules-based approach—which means adherence to the letter of the law—to a more flexible ethical one which is concerned with adherence to the spirit of the law. And this proposes a link between an ethically correct attitude and the activity of compliance, which has been frequently emphasised and studied by numerous authors (Paine 1994; Laufer and Robertson 1997; Treviño et al. 1999; Jackman 2001; Weber and Fortun 2005), who all stress the importance of supporting compliance programmes by a solid orientation towards ethical behaviour and demonstrate that the objective of responsible conduct cannot be achieved solely by imposing from outside what is required but must also appeal to what is desired (Michaelson 2006). They suggest adopting compliance programmes that are not oriented towards mere respect of the rules, but to pursuing the creation of a sense of shared values that can help define an ethical role for individuals, a combination of compliance and values approaches is ideal.

There has been the risk of an exclusive orientation to compliance in the US (Weaver and Treviño 1999) with the Sentencing Commission's guidelines for organisational defendants (Dalton et al. 1994; Weaver et al. 1999) that took effect in 1991, and through which organisations that proactively manage legal compliance face significantly reduced fines and sentences if they are caught engaging in misconduct. Therefore, while many companies have taken a legal compliance approach in their programmes, this has not avoided unethical and illicit behaviour such as Enron and the more recent financial scandals. An illusion of ethical progress has been created which has confused the relationship between ethics and compliance.

This becomes clearer if we compare studies focused on the introduction of a code of ethics, as a written expression of organisational values and beliefs: some studies found that the existence of a corporate code significantly reduced unethical decisions (Hegarty and Sims 1978), while other studies (Laczniak and Inderrieden 1987; Mathews 1987) found that codes have little effect upon decision making or the amount of illegal activity. This demonstrates that a code of ethics is a tool, it is compliance, but it is not the organisational value of the company. Ethical is more

than being merely compliant; compliance is ordinarily a necessary but insufficient condition for ethics.

Moreover, for more than 20 years, researchers from many disciplines have examined the variables that influence business managers when making ethical decisions, but have not yet reached a deterministic certainty, and probably never will, about how to define ethical behaviour. Scholars have identified and explored individual and situational variables that impact ethical decision making in organisations (Loe et al. 2000). Individual variables include the level of cognitive moral development (Treviño and Youngblood 1990), age (Brady and Wheeler 1996), gender (Whipple and Swords 1992), locus of control (Singhapakdi and Vitell 1990) and the level of education (Kohut and Corriher 1994). Situational variables include job context variables, organisational culture (Jones and Hildebeitel 1995) and environmental influences (McDevitt and Van Hise 2002).

What is lacking is an effective integration between business ethics and compliance programmes. Joshua (2002) states that integration is the ability to put ethical principles into practice, to make the substance of ethics programmes a part of the everyday work activities of employees, at all levels. The characteristics of an integrated ethics programme are the following: it is aligned with an organisation's mission and vision; it fits well with organisational systems, policies and practices; it addresses leadership priorities as well as employee expectations for ethics; it is used by employees at all levels to help guide decision making and action; and it becomes a central part of an organisation's culture over time.

Citing several case histories, Paine (1994) found that ethics programmes can emphasise values or can emphasise legal compliance, control and discipline. She argued that programmes emphasising values and responsible conduct and following an integrity strategy are likely to have more desirable and long-lasting impacts than programmes founded on rule-compliance. This means combining a concern for the law with an emphasis on managerial responsibility for ethical behaviour. Therefore, she rejects two simpler formulations of the ethics—compliance relationship, what she calls the “correspondence and separate realms views”. The correspondence view suggests that ethics and law are more or less coextensive. If it is legal, it is ethical, so compliance is sufficient for ethics. Conversely, the separate realms view insists on the strict separation of law and ethics and the prioritisation of one over the other (law is prior in the eyes of lawyers, and ethics in the eyes of ethicists). Paine discredits both views by citing several management examples in which law is an important but insufficient guide to ethical conduct, and concludes that the relationship between law and ethics is much more complex than either view. Paine proposes instead the “organisational integrity” thesis, which goes beyond the other views by positioning a class of compliant behaviours as part of a class of ethical behaviours. The strategies too are very different (Fig. 2.3): the compliance strategy has as its objective the prevention of criminal misconduct, it's based on conformity with externally imposed standards, lawyer driven, and it implies implementing activities such as developing compliance standards, training and communication, handling reports of misconduct, conducting investigations, overseeing compliance audits and enforcing standards; the integrity strategy aims to enable responsible

COMPLIANCE	ETHICS
✓ the objective is the prevention of criminal misconduct ✓ It is based on conformity with externally imposed standards ✓ lawyer driven ✓ it implies implementing activities such as developing compliance standards, training and communication, handling reports of misconduct, conducting investigations, overseeing compliance audits, and enforcing standards;	✓ the objective is to enable responsible conduct ✓ it is based on self-governance according to chosen standards ✓ management driven ✓ it implies implementing activities such as leading company development through values and standards, training and communication, assessing values performance

Fig. 2.3 Compliance versus ethics

conduct and is based on self-governance according to chosen standards, management driven with the aid of lawyer and human resources and it implies implementing activities such as leading company development through values and standards, training and communication, assessing values performance, identifying and resolving problems and overseeing compliance activities.

A broader survey study of Fortune 1,000 firms (Weaver et al. 1999) also found evidence of these two different orientations towards formal ethics management. Adoption of a compliance orientation, which emphasises rules, monitoring employee behaviour and disciplining misconduct, was found to be influenced by executives' awareness of the United States Sentencing Commission's guidelines as well as top management's commitment to ethics. Adoption of a values orientation, which emphasises support for employees' ethical aspirations and the development of shared values, was found to be influenced only by top management's commitment to ethics. In a compliance orientation, rules are imposed from "outside" the employee, rather than resulting from values with which all organisational members identify. They constitute a top-down imposition, rather than identification and internalisation processes. The ethical role identity is created by the fear of discipline for non-conformity. Conversely the values orientation may frame the way employees understand the purpose of compliance activities. When a values orientation is strong, compliance activities can be perceived as part of an overall system of support for ethical behaviour. Without a strong values orientation, compliance activities may be perceived to be part of a system aimed only at detecting misconduct.

Thus, these reflections suggest that it is not optimal to merely establish and enforce the rules. In this context, the creation of symbolic structures is especially attractive: an organisation can point to structural change as evidence of its compliance, without necessarily creating significant change in behaviour, even though the creation of symbolic structures is only the first stage of organisational response to law. Rather, managers need to create a sense of shared values that can help define an ethical role identity for employees and set forth organisational support for employees as an ideal. This needs a continuous effort to incorporate ethics into business, integrating ethics into all daily decision making and work practices for all

employees; Purcell (1977) and Weber (1981) called this “*the institutionalization of ethics into business*”.

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