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Managing ethical performance in organizations: Insights from the corporate world

ABSTRACT

Medical organizations can learn at least three lessons from the recent spate of corporate scandals and the regulatory response they triggered. One is the importance of identifying and eliminating those conflicts of interest that pose unacceptable risks to an organization's reputation or to an industry's public profile. Second, although disclosing a risk attendant to a conflict of interest is of crucial importance, disclosures are not automatic absolutions, regardless of how full and complete they may be. Third, an organization's ethical performance is first and foremost a function of its culture. If there were any doubt, the likes of Enron Corporation and WorldCom confirmed that formal controls and legal sanctions are no substitute for the importance that members of an organization accord to playing by the rules and working with integrity.

I approach this subject from a corporate perspective; although a business school professor at present, my career began in public accounting and included service as a chief financial officer in the securities industry. And although my experience with medical research institutions is quite limited, I have observed that struggles to manage conflicts of interest in the corporate realm bear more similarities than differences with those that confront managers of not-for-profit organizations.

Using recent corporate scandals as examples, I will address a few issues that might be pertinent to medical organizations:

- How to determine which conflicts of interest cannot be managed and must be eliminated
- The limitations of risk disclosures
- The importance of fostering a positive ethical culture, and some ideas on how to do so.

For a more complete discussion of these issues, readers are referred to the report entitled *Embedding Ethics in Business and Higher Education: From Leadership to Management Imperative*.[1]

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WHICH CONFLICTS TO ELIMINATE?

Conflicts of interest are ubiquitous facts of organizational life. Fortunately, most of them can be managed without any untoward consequences. In other words, the possibility that the conflict will give rise to unethical conduct can be reduced through a combination of oversight, sanctions, and incentives. However, some conflicts present temptations too seductive to resist, regardless of how assiduously they are managed. In other cases, a practice appears to represent a conflict in opposition to an organization's professed duty to its customers or patients, regardless of whether the practice is genuinely hazardous or not.

The corporate world has produced some vivid examples of how important it is to identify and eliminate unmanageable conflicts of interest before they damage the reputation of an organization or the standing of an entire industry. A method for distinguishing manageable from unmanageable conflicts is to ask questions such as the following:

- Would our reputation survive a *candid* disclosure of this practice, one that included its true nature and our genuine motivations for seeing it persist?
- What are the chances that we could convince the public that what appears to be a pernicious conflict of interest is actually innocuous?

Conflicts that cannot be candidly disclosed

The insurance brokerage division of Marsh & McLennan Companies was mired in scandal when the attorneys general of several states filed complaints of bid rigging and deceptive uses of contingent commission agreements (ie, arrangements whereby an insurance company rebates a portion of the premium to the broker). In his public statement, the Massachusetts attorney general observed that although Marsh had disclosed the existence of contingent commission agreements, the company had consistently concealed their "true nature." Such obfuscation was not surprising, since to lay out the "true nature" of these practices and Marsh's motivation for them would have been an exercise in self-indictment. In effect, they would have had to say something along the lines of, "Notwithstanding the trust we elicit and the values we profess, we engage in sneaky practices for selfish reasons."

Clearly, if candidly disclosing the true nature of a conflict would impair an organization's reputation, then the practice giving rise to the conflict is a good candidate for elimination.

Conflicts that cannot be defended

As Dr. Thomas Stossel argued earlier in this conference, conflicts of interest in medical research are often quite innocuous and have little or no influence on many patients' willingness to undergo treatment. Nevertheless, the absence of bad intent may not protect against institutional embarrassment and reputational harm. Depending on the severity of public attitudes, eliminating the conflict might represent the best option. The accounting industry provides a case study of the perils of acting otherwise—ie, that persisting in the face of public concern, whether such concern is justified or not, invites a potentially intrusive regulatory response.

The accounting industry's experience bears attention: Failure to manage conflicts of interest can trigger a ferocious regulatory response.

Accounting firms' practice of consulting for their audit clients was controversial before the series of corporate scandals involving Enron Corporation, WorldCom, and Arthur Andersen LLP. Some observers supported the practice because it provides greater insight. Others opposed it on grounds that the quest for consulting fees would impair an auditor's independence. Years ago an effort was made to diffuse the controversy by striking a compromise: footnote disclosure of the consulting fees paid to the auditor. That requirement was lifted several years later after a showing that the disclosure had no influence on investor behavior.

Fast forward to December 21, 2001, when Enron declared bankruptcy. Shortly thereafter, the notion that gargantuan consulting fees had compromised Andersen's audits of Enron went from a working hypothesis to received wisdom. Seven months later, Congress passed and the president signed into law the Sarbanes-Oxley Act, portions of which severely impacted the accounting profession. The act went far beyond the typical device for regulating capital market activity (ie, disclosure) by barring the provision of consulting services to audit clients.

Time will tell whether this constraint is positive or not. I mention it here because the experience of the accounting profession bears the attention of the biomedical community. The accounting industry's failure to manage its conflicts of interest—perceived or real—triggered a ferocious regulatory response. The stakes of managing such conflicts could not be higher—a fact that is hard to appreciate until one's own profession is on the receiving end of hastily drafted legislation.

To draw one more insight from this episode, most conflicts of interest emanate from practices that have a beneficial side. For this reason, elimination of conflicts often can be expected to engender some costs, both predictable and unintended. One possible consequence—certainly relevant to biomedical research—is that the profession's long-term attractiveness and its ability to lure top talent may be compromised.

DISCLOSURE IS NO PANACEA

Throughout this conference there have been numerous mentions of disclosures and what counts as adequate and complete. Although this is a crucial consideration, I would caution against loading too much ethical weight on the fact that a risk was revealed.

Necessary but not sufficient

The motivation for disclosure is something along the lines of "forewarned is forearmed." In reality, some warnings do not arm. If the warning concerns a complex practice whose attendant disclosure is equally complicated, then the patient (or customer, investor, etc.) should not be expected to accurately assess his or her risk. This is especially true in medicine, where trust in their physician will incline most patients to discount the risks and exaggerate the benefits of a proposed therapy. Simply put, physicians are ethically bound to care for the health of their patients, a duty that is not discharged by enumerating risks alone.

Do disclosures change behavior?

To return briefly to the example from the accounting industry, consulting fee disclosures were discontinued because they were being ignored. They produced no measurable impact on financial statement users. This was not an altogether surprising finding since investor trust in the representations of public accountants has been rewarded over time. One would not expect it to erode over the disclosure of an arrangement that had existed for decades.

This raises a similar issue in the biomedical context: Do clinical research participants care about investigators' financial arrangements? Even assuming that the participants may want to know, would they act differently with that knowledge? These are questions that deserve formal research. I conducted some research of this type on a crudely informal basis by describing a financial arrangement between a research physician and a medical device manufacturer and asking a few people whether such an arrangement would affect their decision to proceed with treatment from that physician. Most people I queried said that it would not because their reasons for seeking the treatment would be more important. Some said that the knowledge of a conflict of interest might prompt them to seek a second opinion; for obvious reasons, this may or may not be a wise reaction.

My point is that the quest to "cover the bases" with increasingly complex disclosures of financial arrangements may or may not have the desired result. If patient welfare is the ultimate goal of risk disclosures, then the way patients typically respond to these documents deserves greater study. We should not assume that disclosures are performing a function without empirical evidence to back it up.

Without systematic management of ethical performance, calls for ethical conduct are little more than cheerleading.

FOSTERING ETHICAL PERFORMANCE: LESSONS FROM CORPORATE SCANDALS

Recent corporate scandals have been carefully documented by a variety of outside experts. These "organizational autopsies" contain several lessons applicable to the academic medical center that is intent on improving its ethical performance, by which I mean the extent to which it satisfies the ethical expectations of its stakeholders and society writ large.

Leadership is necessary but insufficient

The ethical tone of an organization is set at the top. But although a highly ethical leadership is vital, it does not guarantee ethical performance. This is particularly true in complex organizations with multiple leaders, in organizations that sprawl geographically, and during times of organizational instability. In short, without systematic management of ethical performance, calls for ethical conduct are little more than cheerleading.

Culture trumps compliance

Failures along the lines of Enron and WorldCom are case studies in the limits of compliance efforts, be they internal controls, outside gatekeepers, or the vast array of oversight systems (eg, whistleblower hotlines). Among the reasons for these catastrophic breakdowns is one that cannot be eliminated: compliance mechanisms are only as good as the culture in which they operate. Said another way, culture trumps compliance.

As long as organizations are comprised of people, unethical conduct will be a fact of organizational life. However, those organizations with positive ethical cultures self-correct from such conduct and grow stronger as a result. In contrast, the same conduct can destroy an organization with a degenerate culture because instead of repelling and correcting the behavior, the culture reinforces it.

The notion that ethical culture is of overarching importance is the one finding that cuts across all of the scandalous failures of recent years. But it can also be gleaned from the reaction of the US Sentencing Commission to these same episodes. An advisory group to the Commission dealt with the uncomfortable finding that Enron and WorldCom would have received favorable culpability scores. That is, both organizations had in place the sort of controls that would have ameliorated any fines for criminal fraud. Boldly, the Commission asked, "What did we miss?" The answer—"the culture"—is contained in the report of the Ad Hoc Advisory Group on the Organizational Sentencing Guidelines (October 2003).[2] Thus, whether or not one accepts this conclusion, the ethical culture of an organization will be considered in future culpability score calculations.[3]

COMPONENTS OF MANAGING ETHICAL CULTURE

Creating and maintaining a positive ethical culture requires proactive management efforts. As with any important objective, managers carrying out these efforts need detailed goals, proper incentives, and the resources to succeed. I have discussed what this entails in a previous publication;[1] the key elements are as follows:

- The organization's baseline ethical culture must be assessed.
- Those with operating responsibility should be assigned the task of managing the assessment. If the culture is acceptable, then they should maintain it in that condition; if the culture could stand improvement, then they should have clear targets.
- Through successive assessments, a manager assigned this responsibility should be held accountable for the results—ie, his or her compensation

should reflect whether goals are achieved.

- In addition to systematic management of the culture, it is often necessary to harmonize an organization's strategy and tactics with the ethical expectations of key stakeholders and society generally. More times than not, this will require elimination of pernicious conflicts of interest and similarly corrosive practices.
- Ideally, efforts should be made to cause the ethical condition of the organization to become as transparent as possible. Insofar as this factor is the one piece of information that is predictive of ethical performance, board members and other interested parties would be well advised to demand it.

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