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Out of Touch

THE CEO'S ROLE IN CORPORATE MISBEHAVIOR*

Linda Klebe Treviño[†]

I. INTRODUCTION

The last few years have brought an endless parade of headlines and “perp walks,” raising questions about who is to blame for an apparent spike in corporate misbehavior. In this paper, I rely on social-scientific theory and empirical research to focus on the role of the CEO in corporate misconduct. I demonstrate, first, that an active CEO role in ethics management is essential because the CEO's commitment to ethics influences key characteristics of formal ethics and legal compliance programs. In addition, as Chief Ethics Officer, CEOs must create and maintain the ethical culture in their organizations. Both of these types of influence can have a powerful impact on employee behavior. However, research also suggests that many CEOs are out of touch with the importance of their ethics management role. Senior managers tend to view the firm's ethical climate in “rosy” terms compared to lower-level employees. In addition, many CEOs become far removed from the ethical realities in their organizations simply because they rarely interact with lower-level employees. As a result, their organizations and employees are left to flounder without a strong rudder to guide the organization in an ethical direction.

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One very pragmatic reason to focus on the CEO role has to do with the U.S. Sentencing Guidelines compliance standards.¹ The guidelines were first adopted in November 2001 to reduce judicial discretion and to provide a “carrot and stick” approach to sentencing corporations convicted of crimes. In the “carrot” part of the approach, the original Sentencing Guidelines called for leniency in sentencing organizations that can demonstrate that they had made a strong effort to prevent employee misconduct. The guidelines listed seven standards for judging what would be considered an “effective” legal compliance program, including: high-level executive oversight of the firm’s efforts to insure legal compliance, the exercise of care in delegating this authority to others, communication of conduct standards through dissemination, and regular employee training. The guidelines also included requirements regarding the establishment of systems to monitor employee behavior, including systems that allow employees to report misconduct they observe as well as consistent discipline for misconduct when it occurs, and responses to misconduct that are designed to prevent its reoccurrence. A 2003 survey found that most large organizations had formal ethics or legal compliance programs.² The study found that the larger the organization, the more likely it was to have formal codes, ethics training, ethics offices or advice lines, and anonymous reporting systems.³

Ideally, the CEO’s role should be important in guiding the establishment and implementation of these programs. However, in practice, most large firms that implemented legal compliance programs in the 1990s delegated authority for these formal programs to an “ethics or compliance officer”—the Chief Legal Counsel or another executive appointed to manage internal ethics and legal compliance programs. Many of these officers belong to the Ethics Officers Association (EOA),⁴ a professional organization that has grown through the 1990s to its current size of over 1000 members. Although members of the EOA meet regularly to benchmark and discuss best

¹ See UNITED STATES SENTENCING COMMISSION, FEDERAL SENTENCING GUIDELINES MANUALS, at www.ussc.gov/GUIDELIN.HTM (last visited April 20, 2005).

² NATIONAL BUSINESS ETHICS SURVEY 6 (Ethics Resource Center ed., 2003) [hereinafter SURVEY].

³ *Id.*

⁴ See ETHICS OFFICERS ASSOCIATION (EOA), *About the EOA*, at <http://www.eoa.org/AboutEOA.asp> (last visited April 20, 2005).

practices in ethics and legal compliance management, research suggests that the large majority of ethics/compliance officers have little regular contact with the CEO,⁵ calling into question how active CEOs are in guiding ethics and compliance management efforts.

A number of observers became concerned over the years that some of these formal ethics/legal compliance programs were little more than “check-off” efforts that allowed organizations to say that they were in compliance with the Sentencing Guidelines while, in fact, the programs were seen by employees as little more than window dressing. Perhaps because of these concerns, changes to the U.S. Sentencing Guidelines, as of November 1, 2004, further highlighted the role of senior executives in creating a strong ethical culture in the firm in addition to a formal ethics or legal compliance “program.” These changes require that the “governing authority” be knowledgeable about and exercise reasonable oversight regarding the implementation and effectiveness of the ethics or compliance program, and that the organization “promote an organizational culture that encourages ethical conduct and commitment to legal compliance.” In addition, Sarbanes-Oxley has increased the accountability of both senior executives and the board for the oversight of financial reporting. As a result, CEOs and boards have taken more interest in the implementation of ethics/compliance programs in their firms and are asking more questions about what their role should be in promoting an organizational culture that encourages ethical conduct and commitment to legal compliance.

Fortunately, empirical research conducted over the past ten years provides some guidance. First, such research demonstrates clearly that CEOs matter. Their personal commitment to ethics influences characteristics of formal ethics and legal compliance programs. In addition, their leadership has a powerful influence on the creation and maintenance of ethical cultures in their organizations.

⁵ See Gary R. Weaver et al., *Corporate Ethics Practices in the Mid-1990s: An Empirical Study of Fortune 1000*, 18 J. BUS. ETHICS 283, 283-94 (1999).

II. CEO INFLUENCE ON FORMAL ETHICS/COMPLIANCE PROGRAMS

Research has found that the CEO's "commitment to ethics" influences the scope, orientation, and integration of the formal ethics/compliance program.⁶ Ethics and legal compliance programs can be conceptualized as organizational control systems that aim to control employee ethical and legal conduct. As suggested above, these programs generally include some or all of the following elements: ethics or legal compliance officers, formal codes of conduct, training programs, systems for reporting misconduct, and disciplinary mechanisms for handling unethical or illegal behavior. Previous studies had generally documented the existence of such programs and elements, but had not attempted to differentiate among them in terms of their "scope."⁷

Programs have also been discussed in terms of their control orientation. Programs may rely on a coercive approach to controlling employee behavior that is based upon rules, monitoring for rule compliance, and discipline for rule infraction—a compliance-based approach. Alternatively, programs may attempt to control employee behavior in a more aspirational manner by creating commitment to shared ethical values—a values-based approach. These approaches need not be mutually exclusive. In fact, in many organizations they are designed to work together. Programs can work to develop shared values, support and encourage employees whose behavior is consistent with those values, while holding others accountable for behavior that is inconsistent with the values.⁸

Finally, programs can be differentiated in terms of the level of their integration with daily organizational activities. Some may be highly integrated programs that affect everyday decisions and actions in the organization, while other programs

⁶ See Gary R. Weaver & Linda Klebe Treviño, *Compliance and Values Oriented Ethics Programs: Influences on Employees' Attitudes and Behavior*, 9 BUS. ETHICS Q. 325, 325-45 (1999) [hereinafter *Compliance*]; Gary R. Weaver et al., *Integrated and Decoupled Corporate Social Performance: Management Commitments, External Pressures, and Corporate Ethics Practices*, 42 ACAD. MGMT. J. 539, 539-52 (1999) [hereinafter *Integrated*].

⁷ Scope of a program is defined as the number of different program elements that a particular organization includes in its formal program.

⁸ See Lynn Sharp Paine, *Managing for Organizational Integrity*, 72 HARV. BUS. REV. 106, 106-17 (1994); Linda Klebe Treviño et al., *Managing Ethics and Legal Compliance: What Works and What Hurts*, 41 CAL. MGMT. REV. 131, 131-51 (1999) [hereinafter *Managing Ethics*].

are perceived to be little more than window dressing. Organizational researchers refer to the latter as “decoupled” programs because they operate in a way that has little influence on daily decisions and behavior. These programs may look good from the outside, but members of the organization recognize that they have little impact on daily organizational functioning. So, for example, an organization may develop and distribute a code of conduct, but do little to enforce it. As a result, the code gathers dust or ends up “filed” in the circular file.

If they were asked directly, most CEOs would likely say that they are highly committed to ethics. But the more important questions are whether employees perceive that commitment, and whether the CEO’s commitment to ethics is seen as high relative to the executive’s commitment to other, more bottom-line oriented concerns. In my research with colleagues, we hypothesized that the CEO’s commitment to ethics would be associated with increased program scope (the existence of more formal ethics/compliance program elements), a higher likelihood that the program would be values-oriented (rather than compliance-oriented), and the likelihood that the program would be integrated into daily organizational activities such as performance appraisal systems. We asked ethics/compliance officers to rate the CEO’s commitment to ethics relative to other operational and strategic concerns, and we found that, as proposed, the CEO’s commitment to ethics was associated with program scope, orientation, and integration. In organizations with strong CEO commitment to ethics, we found more formal program elements, a stronger values orientation in those programs, and greater integration of the formal program into daily organizational life.⁹

It is particularly important to focus on these program characteristics because research has also found that they make a difference in employee outcomes. First, employees who work for organizations that have formal ethics and legal compliance programs with multiple program elements are more likely to say that they would report misconduct and are less likely to report feeling pressure to compromise ethical standards or to say that they have recently observed misconduct in their organization.¹⁰ Even more important, however, than formal

⁹ See *Compliance*, *supra* note 6; *Integrated*, *supra* note 6.

¹⁰ See generally SURVEY, *supra* note 3.

program elements are a values orientation and integration of the program into daily organizational life. Research has found that these aspects of ethics and compliance management have a stronger impact on employee attitudes and behaviors than do the existence of formal program elements.¹¹ Employees respond best to a formal program that has a primary values orientation backed up by a system of accountability. Attention to shared values (e.g., integrity, respect, etc.) creates norms and behavioral expectations, but it may also help to create shared trust and a perception of organizational support. In addition, employees want to know that when values and rules are violated, the organization will hold the violator accountable.¹² Accountability contributes to perceptions that the organization is fair and means what it says with regard to ethics.¹³ In empirical research, employee perceptions that the ethics/compliance program was primarily values-based were positively associated with, among other outcomes, employees' awareness of ethics at work, their willingness to seek ethical advice in the organization, their commitment to the organization, willingness to report misconduct, and lower-observed misconduct. Although a perceived compliance focus was also associated with positive outcomes, a values orientation was the more important influence in every case.¹⁴

Finally, employee perceptions that ethics and legal compliance programs are integrated into the daily life of the organization are also important. For example, if employees perceive consistency between formal policies and programs and organizational practices, and believe that the organization follows up on ethical concerns reported by employees and works hard to detect misconduct, employee outcomes are more positive.

In sum, we see that senior leadership is important because it influences the scope, orientation, and integration of formal ethics and compliance programs. To the extent that the CEO is highly committed to ethics, the organization includes more formal program elements in its ethics and legal

¹¹ See *Managing Ethics*, *supra* note 8.

¹² See *id.*; *Compliance*, *supra* note 6.

¹³ See Linda Klebe Treviño, *The Social Effects of Punishment: A Justice Perspective*, 17 ACAD. MGMT. REV. 647, 647-76 (1992).

¹⁴ See, e.g., LINDA KLEBE TREVIÑO & GARY WEAVER, *MANAGING ETHICS IN BUSINESS ORGANIZATIONS: SOCIAL SCIENTIFIC PERSPECTIVES* 211 (2003); *Managing Ethics*, *supra* note 8; *Compliance*, *supra* note 6.

compliance management, the program is more values-oriented in its focus, and is more integrated into the daily life of the organization. These program characteristics are all associated with positive employee outcomes, including reduced levels of misconduct and higher willingness to report misconduct when it is observed. But the emphasis on integration also suggests that the best outcomes are achieved when ethics are perceived to be integral to the overall organizational culture and not just another program (because programs come and go in organizations).

III. CEO INFLUENCES ON AN ORGANIZATION'S ETHICAL CULTURE

We have now seen that senior executives influence the characteristics of formal ethics management. Yet creating a formal ethics or legal compliance program, by itself, does not guarantee effectiveness. Recall that Enron had an ethics code and other aspects of a formal program. Not surprisingly, research suggests that employees must perceive that formal policies are consistent with the real ethical culture of the organization. For formal systems to influence behavior, they must be part of a larger, coordinated cultural system that supports ethical conduct every day.

Culture can be defined as a body of learned beliefs, traditions, and guides for behavior that are shared among members of a group.¹⁵ This idea of culture has been used extensively to understand work organizations and the behavior of organizational members.¹⁶ Organizational culture is thought to be important because it has a powerful impact on employee behavior. Leaders influence culture by portraying a vision, by paying attention to, measuring, and controlling certain things, by making critical policy decisions, by recruiting and hiring personnel who fit the vision and values of the organization, and by holding people accountable for their actions.¹⁷ So, for example, CEOs who care about ethics will include ethics in their vision of the organization. They will design a reward

¹⁵ RICHARD A. BARRETT, *CULTURE AND CONDUCT: AN EXCURSION IN ANTHROPOLOGY* 54 (1984).

¹⁶ TERRENCE E. DEAL & ALLAN A. KENNEDY, *CORPORATE CULTURES* 107-27 (1984).

¹⁷ EDGAR H. SCHEIN, *ORGANIZATIONAL CULTURE AND LEADERSHIP* 223-37 (1985).

system that values and measures both means and ends, and, because they will be concerned about sending the right messages to employees, they will use discipline wisely.

Ethical culture can be thought of as a component or slice of the overall culture of the organization. Ethical culture provides informal as well as formal systems in a complex interplay that either supports ethical or unethical conduct.¹⁸ Formally, messages from executive leadership, organizational structure, selection systems, orientation and training programs, rules and policies, formal reward and performance appraisal systems, and decision-making processes all contribute to ethical culture creation and maintenance. The ethics programs discussed earlier can be thought of as part of the formal cultural systems. Employees are introduced to codes of conduct, ethics training programs, and systems for reporting misconduct. But how they think about and respond to these is highly dependent upon other, mostly informal, cultural systems. Informally, the culture's norms of daily behavior, heroes, rituals, stories, and language keep the ethical culture alive and indicate to both insiders and outsiders whether the formal systems are actually implemented or are merely a façade. I will not discuss all of these ethical culture components separately because they are extensively covered elsewhere.¹⁹ Rather, I will focus on the ethical leadership role of the CEO because CEOs set organizational priorities (including funding priorities), contribute to the design of organizational systems, and send powerful messages about valued behavior through their ongoing communications and actions. Messages about ethics flow from the top down in organizations and the CEO is the source of many of those messages.

So, what do we know about CEOs and ethical leadership? Recent research suggests that executive ethical leadership in large business organizations is a reputational phenomenon.²⁰ Most employees observe senior executives from a distance rather than through direct interaction. As a result, they form impressions of the senior executive's ethical stance

¹⁸ LINDA KLEBE TREVIÑO & KATHERINE A. NELSON, *MANAGING BUSINESS ETHICS: STRAIGHT TALK ABOUT HOW TO DO IT RIGHT* 255 (3d ed. 2004).

¹⁹ *See id.*

²⁰ *See* Linda Klebe Treviño et al., *Moral Person and Moral manager: How executives develop a reputation for ethical leadership*, 42 CAL. MGMT. REV. 128, 128-142 (2000); Linda Klebe Treviño et al., *A Qualitative Investigation of Perceived Executive Ethical Leadership: Perceptions From Inside and Outside the Executive Suite*, 56 HUM. REL. 5, 5-37 (2003) [hereinafter *Qualitative Investigation*].

from afar. And, to develop a reputation for ethical leadership, executives must be perceived to be both “moral persons” and “moral managers.” These two dimensions combine to create an ethical leadership matrix with ethical leaders being high on both dimensions (see Figure 1).

Figure 1: Executive Ethical Leadership Reputation Matrix

| | | <u>Moral Person</u> | |
|----------------------|--------|----------------------------|------------------------------------|
| | | Weak | Strong |
| <u>Moral Manager</u> | Strong | Hypocritical Leader | Ethical Leader |
| | Weak | Unethical Leader | Ethically neutral leader →? |

The moral person dimension represents the individual traits ascribed to the executive by employees. CEOs who are seen as moral persons are thought to be honest, open, trustworthy, concerned about people, personally moral, as well as fair and principled in their decision making. Because they realize that employees are watching them for cues about appropriate behavior, those who are also moral managers make it a point visibly to role model ethical conduct and to communicate an ethics and values message. In addition, moral managers use the reward system to support ethical behavior and discipline unethical behavior.

In fact, because a reward system lets employees know what is truly important, it is one of the most important cultural systems that can be influenced by the CEO's ethical leadership. Employees know that observing who gets ahead (and who doesn't) and how rewards and discipline are allocated in an organization is probably the best indicator of what really matters. Simply put, what is rewarded is what gets done. If salespeople are rewarded on commission only, it should be no surprise that salespeople will lie to make a sale. Or, if commissions are higher for some products than for others, salespeople can be expected to push those products even if they don't fit customer needs. Although people don't expect to be

rewarded for being ethical, some ethical leaders are sending important cultural messages by rewarding ethical behavior. For example, at Lockheed Martin, the chairman instituted a “Chairman’s Award” for exemplary ethical conduct. The award is given annually at a meeting of 250 senior managers. Each of these senior leaders is expected to nominate someone each year—meaning that, at the highest organizational levels, senior leaders are looking for exemplary ethical conduct to reward. The award ceremony has become a cultural ritual and stories about the winners and runners up are distributed to all employees via the company newsletter.²¹

How senior leaders react to unethical behavior is also extremely important. In his book, Thomas Watson, Jr., the son of IBM’s founder, told a story about the importance of disciplining unethical behavior and the message it sends to employees.²² Under his leadership at IBM, a group of managers started a chain letter that eventually found its way to employees who felt pressure to join so that managers would get their payoff. When Watson learned about it, he wanted heads to roll, but he couldn’t convince the division head to fire any of the managers involved. A couple of years later, the company fired a low-level employee for stealing engineering drawings and selling them. Unfortunately, the firing was handled poorly and the fired employee made Watson’s life miserable for years based upon the fact that the company had failed to fire anyone in the earlier chain letter situation. Watson learned his lesson, saying that after this experience, he always fired managers who failed to act with integrity, and that included very senior managers. He often had to overrule other managers who preferred lesser punishment. In the end, though, the company was better off because the clear message that was sent to everyone was that integrity really does matter.²³

According to the matrix,²⁴ a leader who is strong on both the moral person and moral manager dimensions is perceived to be an *ethical leader*. Founders are often credited with establishing a culture that continues in the organization long after they are gone. Interestingly, Arthur Andersen, the founder of the now defunct auditing firm, was an exemplar of

²¹ See TREVIÑO & NELSON, *supra* note 18.

²² See THOMAS J. WATSON JR., *FATHER SON & CO.: MY LIFE AT IBM AND BEYOND* (1990).

²³ See *id.*; TREVIÑO & NELSON, *supra* note 18.

²⁴ See *supra* figure 1.

ethical leadership. Among other attributes, Andersen was known as a highly ethical person who also led his employees to operate with strong ethics and values. Stories about the founder's personal ethics were told and retold. For example, a young Arthur Andersen, at the age of twenty-eight, confronted a railway executive who demanded that his books be approved or he would pull his business. Andersen said, "there's not enough money in the city of Chicago to induce me to change that report."²⁵ The railway company later filed for bankruptcy and Arthur Andersen became known as a firm one could trust. Andersen also taught employees his mother's challenge to "think straight—talk straight"²⁶ and the phrase became a corporate mantra. Partners said proudly "that integrity mattered more than fees."²⁷ That culture was maintained by subsequent ethical leaders for decades.

A leader who is low on the moral person and moral manager dimensions is perceived to be an *unethical leader*. While at Sunbeam, Al Dunlap lied to Wall Street about the firm's financial state and became known for his "emotional abuse" of employees. He also pressured employees to use questionable accounting and sales techniques in order to meet bottom-line goals. He crippled the company before the board fired him in 1998.²⁸

Leaders who talk the ethical talk (they are moral managers), but don't walk the walk (they are not moral persons), are seen as *hypocritical leaders*. Such leaders talk about integrity, but their conduct tells a different story. Hypocritical leadership is about ethical pretense—putting on a good show. As the founder of PTL Ministries, Jim Bakker preached about doing the Lord's work while he raised funds for lifetime memberships in his Heritage USA Christian theme park. He diverted millions of dollars in donations and memberships to support PTL operating expenses and a lavish lifestyle for family and associates. PTL went bankrupt in 1987 and Bakker spent eight years in prison.²⁹ Hypocritical leaders create cynicism in employees. Why should an employee reject a gift from a vendor (as the code of ethics requires) when the

²⁵ BARBARA LEY TOFFLER, *FINAL ACCOUNTING: AMBITION, GREED AND THE FALL OF ARTHUR ANDERSON* (2003).

²⁶ *Id.*

²⁷ *Id.*

²⁸ John A. Byrne, *Chainsaw*, 18 BUS. WEEK 128, 128-49 (1999).

²⁹ G. Tidwell, *Accounting for the PTL Scandal*, TODAY'S CPA, July-Aug. 1993.

CEO regularly sits in an expensive stadium seat that is provided by a key client?

The final category, ethically neutral leadership, is the most controversial with executives. It applies to executives who fall into what employees perceive to be an ethically neutral zone. They may be ethical persons, but followers aren't really sure because the executive fails to "lead" in the ethics arena. The ethically neutral leader isn't unethical, but he isn't visibly ethical either. He fails to be a conscious ethical role model, and tends to focus on bottom-line goals without equal attention to how these goals are achieved. Essentially, the leader is silent about ethics and that silence is interpreted to mean that the top executive must not care as much about ethics as she or he does about issues that get more attention. Business leaders don't like to think that their employees perceive them as ethically silent or neutral. They think, "I can't be ethically neutral—I'm making tough ethical decisions all the time!" And they are. The problem is that most employees don't know what they're thinking or how those decisions are made unless they choose to communicate with employees.

A *Fortune* magazine writer referred to Sandy Weill, former CEO of Citigroup, as "tone deaf" on ethics issues. Weill's management philosophy led him to decentralize and delegate management of the firm's many business units. It appears that ethics management was delegated along with everything else. Arguably, the firm was lacking a strong rudder to guide it in a highly competitive business environment. As a result, Citigroup was implicated in a number of scandalous allegations and has spent a great deal of time and energy over the past few years responding to ugly headlines.³⁰

Interestingly, the current CEO, Chuck Prince, who is beginning his second year as chief executive, has been much more proactive in the moral manager role. He seems to understand the importance of ethical leadership in a way that his predecessor did not. Prince has a sign on his desk that says "No Excuses." He is strengthening formal risk and compliance systems and has vowed to be "ruthless" with rule-breakers. At a minimum, he has asked employees to know the rules that govern their own work. But he has also begun talking about values and the need for employees to internalize good ethics.³¹

³⁰ Carol J. Loomis, *Whatever it Takes*, FORTUNE, Nov. 25, 2002, at 74-75.

³¹ Mitchell Pacelle, *Citigroup CEO Makes "Values" A Key Focus; Prince Veers*

So, being an executive who is perceived to be an ethical leader requires more than strong personal character. In order to be an effective ethical leader, executives must demonstrate that they are not only ethical themselves, but they must make their expectations of others' ethical conduct explicit and they must hold all of their followers accountable every day. Research has found that executive ethical leadership is critical to employee behavior. In a recent study, firms that had an ethical culture characterized by top executives who represented high ethical standards, regularly showed that they cared about ethics, and were models of ethical behavior had a lower incidence of unethical behavior. Further, employees in these firms were more committed to their organization, more ethically aware, and more willing to report problems to management.³²

As suggested earlier, some CEOs neglect this important aspect of their responsibility and, as the following quotes from interviews with senior executives show,³³ reject the notion that they could possibly be perceived as ethically neutral:

I don't think there is such a thing as ethical neutrality . . . because I think . . . we are forced to make judgments and decisions that, whether we like it or not, have a moral dimension.

.....

You cannot be ethically neutral. No you can't because you decide every day and ultimately people start to understand. You decide . . . what disciplinary action you're going to take because someone else did not act ethically and everyone's in the room when you make that decision. So how can you be ethically neutral? You decide.³⁴

Although the last quote states that "everyone's in the room," the reality is that there is only a discrete group of individuals in the room when a CEO is making the tough decision about how to discipline unethical conduct. Frequently, only other executives—and certainly not rank-and-file employees—are present. In fact, employees in most organizations will never learn about disciplinary action taken because such actions are considered private personnel matters. As a consequence, senior executives must become much more

from the *Megadeals Done by Weill and Won't Aim Regularly to "Harpoon A Whale"*, WALL ST. J., Oct. 1, 2004, at C1.

³² See *Managing Ethics*, *supra* note 8.

³³ See *Qualitative Investigation*, *supra* note 20.

³⁴ Linda Kebe Treviño et al., *A Qualitative Investigation of Perceived Executive Ethical Leadership: Perceptions From Inside and Outside the Executive Suite*, 56 HUM. REL. 5, 25-26 (2003).

sensitive to the view from the bottom of the organization and the fact that, to be perceived as an ethical leader, their communications and actions must speak loudly about the importance that everyone in the organization behave ethically.

IV. CEOs OUT OF TOUCH

We have now established that the CEO influences the characteristics of formal ethics and compliance programs and the ethical culture of the firm through ethical leadership, and that both of these significantly impact employee attitudes and behaviors. These findings are consistent with the general understanding that CEOs set the “ethical tone at the top.”³⁵ So why aren’t CEOs more directly involved in the management of ethics in their organizations? Research suggests some preliminary answers that help us understand that what one sees and knows is determined by where one sits in the organization.³⁶ First, because of their inclination to identify closely with the organization and its image, top managers have a “rosier” view of their organization’s ethical climate than do lower-level employees. Further, due to fear and futility concerns, employees are unlikely to report ethical problems up the chain. As a result, CEOs are unlikely to know about ethical problems in their organizations. Finally, because most CEOs interact primarily with others of high status, they are likely to be out of touch with the daily realities of their own organizations and employees, including the ethical climate.

Because their own identities are tied to the organization’s identity and image,³⁷ employees tend selectively to perceive the good, ethical side of their organizations more readily than the bad, unethical side. But, as the most senior leader of the organization, CEOs’ personal identities can be expected to be linked even more closely with the identity and image of their organization than are the identities of average employees. The CEO is intensely involved with the organization and its interests, represents the organization to the outside world, and serves as the organization’s agent with

³⁵ See MARSHALL B. CLINARD, *CORPORATE ETHICS AND CRIME: THE ROLE OF MIDDLE MANAGEMENT* 72-89 (1983).

³⁶ Michael G. Pratt & Anat Rafaeli, *Organizational Dress as a Symbol of Multilayered Social Identities*, 409 *ACAD. OF MGMT. J.* 862, 862-98 (1997).

³⁷ Kimberly D. Elsbach & Roderick M. Kramer, *Members’ Responses To Organizational Images and Member Identification*, 39 *ADMIN. SCI. Q.* 442, 447 (1996).

multiple stakeholders.³⁸ Therefore, there is a greater tendency for CEOs to perceive their organization in a positive light as compared with lower-level employees. In fact, research has found that senior managers have significantly more positive perceptions of organizational ethics when compared to rank-and-file employees. Senior managers are less likely to see ethics initiatives cynically and are more likely to perceive the internal ethical environment to be supportive of ethical conduct in the organization. They are also more likely to believe that employees will raise ethical issues and report ethical problems to management.³⁹

Despite their powerful role and place at the apex of the organization, many CEOs base their perceptions of their own organization on highly limited information. Normal organizational communication processes can insulate senior managers from negative perceptions of the organization, keeping them out of touch with lower-level employees on matters of organizational ethics. Research on information processing and upward communication in organizations suggests that senior managers may be somewhat naïve about and protected from the realities of organizational ethics. Upward communication in organizations is frequently filtered and distorted, with information gaps growing larger as the number of intervening hierarchical levels increases.⁴⁰ Research on voice and silence in organizations also suggests that important information, especially negative information, is often withheld from executives. Employees are hesitant to relay unfavorable information up the organizational hierarchy⁴¹ because they fear retaliation or because they believe such efforts to be futile.⁴² Thus, accurate information, especially

³⁸ Jane E. Dutton et al., *Organizational Images and Member Identification*, 39 ADMIN. SCI. Q. 239, 239-63 (1994); Charles W. L. Hill & Thomas M. Jones, *Stakeholder-Agency Theory*, 29 J. MGMT. STUD. 131, 131-54 (1992); S.G. Scott & V. R. Lane, *A Stakeholder Approach to Organizational Identity*, 25 ACAD. MGMT. REV. 43, 43-62 (2000).

³⁹ Linda Klebe Treviño et al., *Comparing Senior Managers' and Employees' Perceptions of Organizational Ethics*, in ACADEMY OF MANAGEMENT ANNUAL MEETING BEST PAPER PROCEEDINGS (2000).

⁴⁰ Fredric M. Jablin, *Superior-Subordinate Communication: The State of the Art*, 86 PSYCHOL. BULL. 1201, 1201-22 (1979).

⁴¹ Charles A. O'Reilly III & Karlene H. Roberts, *Information Filtration in Organizations: Three Experiments*, 11 ORGANIZATIONAL BEHAV. & HUM. PERFORMANCE 253, 253-65 (1974).

⁴² See Elizabeth Wolfe Morrison & Frances J. Milliken, *Organizational Silence: A Barrier to Change and Development in a Pluralistic World*, 25 ACAD. MGMT. REV. 706, 706-07 (2000); Kathleen D. Ryan & Daniel K. Oestreich, *Cycle of Mistrust*, 11

information about organizational problems, is unlikely to find its way up through multiple organizational layers from lower-level employees to senior managers. As a result, many CEOs simply do not have their fingers on the ethical “pulse” of their organizations.

Finally, executives’ association patterns may contribute to this general lack of information from lower-level employees. Some executives choose to engage nearly exclusively in associations with high status communication partners (e.g., other CEOs and other elites) while minimizing associations with parties of low status, especially lower-level employees.⁴³ Such an interaction pattern influences the information that executives have available because executives’ interactions are an important source of social information that influences their interpretations and decision making.⁴⁴ In order to access unfiltered information about the ethical climate and culture, executives must reach out directly and regularly to rank-and-file employees. If they do not, the information they have available about the ethical climate will be highly limited and they may miss information about ethical breaches. Executives can only improve their access to important information from lower-level employees by finding ways to interact with them directly and in regular two-way communication about ethics. Such efforts are more likely to encourage honest input to the CEO about the organization’s ethical climate and culture.

V. CONCLUSION

CEOs contribute to corporate misbehavior in a number of ways. First, CEO commitment to ethics has a powerful impact on the scope, orientation, and integration of formal ethics programs. But many, if not most, CEOs delegate

EXECUTIVE EXCELLENCE 15 (1994).

⁴³ G. Chen et al., *CEO Elitist Association* (2005) (unpublished manuscript, on file with author).

⁴⁴ See, e.g., SYDNEY FINKELSTEIN & DONALD C. HAMBRICK, STRATEGIC LEADERSHIP: TOP EXECUTIVES AND THEIR EFFECTS ON ORGANIZATION 123-30 (1996); Robert M. Grant, *Toward a Knowledge-Based Theory of the Firm*, 17 STRATEGIC MGMT. J. 109, 109-22 (1996); Morton T. Hansen, *The Search-Transfer Problem: The Role of Weak Ties in Sharing Knowledge Across Organization Subunits*, 44 ADMIN. SCI. Q. 82, 82-111 (1999); William H. Starbuck & Frances J. Milliken, *Executives’ Perceptual Filters: What They Notice and How They Make Sense*, in THE EXECUTIVE EFFECT: CONCEPTS AND METHODS FOR STUDYING TOP MANAGERS 42 (1988); Gerald R. Salanick & Jeffrey Pfeffer, *A Social Information Process Approach to Organizational Identity*, 28 ADMIN. SCI. Q. 184, 184-200 (1978).

responsibility for these formal programs to other executives with whom they rarely interact. Second, through their ethical leadership, CEOs are essential to the development and maintenance of a strong ethical culture and climate in the organization. But, again, many CEOs devote too few corporate or personal resources to this effort. Many are more concerned with “checking off” requirements of the U.S. Sentencing Guidelines or the Sarbanes-Oxley Act. Finally, many CEOs are out of touch with the ethical realities of daily life in their organizations because of their close personal identification with the organization, typical organizational communication patterns that block information flow, and their own interaction choices that limit the availability of information from lower-level employees. CEOs who wish to contribute to “good” corporate behavior must commit to being the firm’s Chief Ethics Officer, recognizing the importance of a strong reputation for ethical leadership, and taking responsibility for the development and maintenance of a solid ethical culture.