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## Building an Ethical Corporate Culture to Mitigate Deviant Behavior and Prevent Fraud

How taking a “people perspective” is good for peace of mind and the bottom line

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## Executive Summary

Businesses today face the challenge of dealing with “deviant workplace behavior” which undermines the company’s culture and puts the organization at a higher risk of losses due to decreased productivity, property damage, various forms of liability, and — a major area of concern for our practice — fraud. But, if an organization’s people present a dilemma, they also form the core of the solution. We cite research that has clearly shown that when a company understands the causes of deviant behavior and commits to proactive steps that empower its people to behave ethically, the organization can reduce incidents of deviant behavior, create a more positive work environment, and improve its bottom line. A key component to our plan for building a better organization is to create a company-wide ethics program that articulates the organization’s values, trains employees to uphold and advance those values, and assesses performance based on those values. The positive results businesses can expect include better leadership, better communication, enhanced clarity of purpose, reduced stress, and greater sense of belonging. Within such an environment, employees are less likely to act out against the company and more likely to report violations of the company’s values. This means less deviant behavior, more problems nipped in the bud, and greater protection against losses due to deviant workplace behavior.

## Introduction: Building a Better Organization that Enculturates Better People

Much has been written and said about the coarsening of our popular culture. A cursory glance at social media gives the distinct impression that as a people we are stewing in a toxic brew of perceived injustice, envy, resentment, entitlement, frustration, and seething anger. Of course, we can note that social media is a distortion. By giving free rein to the expression of grievances and allowing hostile exchanges without real-world consequences, the platform reaps what it sows. Those trolls deliberately baiting each other are just as capable of compassion, patience, tolerance, humility and heroism, if given half a chance. That may be generally true, but if you are a business owner, you must be at least a little concerned that what goes on in cyberspace could seep into your office space.

As risk managers, we use the term deviant behavior to describe “voluntary behavior that violates significant organizational norms and, in doing so, threatens the well-being of the organization or its members, or both.”<sup>1</sup> The word “deviant” might be slightly ironic at a time when social norms are falling like dominoes, but behaviors such as sexual harassment, bullying, intimidation, beratement, and theft are still met with universal (theoretical) condemnation, even if they seem to be more commonly practiced. As leaders in ethics, compliance, antifraud programs and controls, and investigations, we have observed that deviant behavior inevitably poisons corporate culture leading to preventable losses: liability for lawsuits, losses due to internal theft and fraud, and expenses associated with “churn” as disenchanting employees leave the company seeking a better environment.

This paper addresses the harm that deviant behavior inflicts on a business and offers solutions gleaned from years of work with countless organizations both large and small. It is our belief that a positive corporate culture that strictly limits deviant behavior reduces the company’s exposure to liability and to internal theft and enables the company to retain valued employees. However, to succeed at building such a culture, management must understand the relationship between deviant behavior and negative outcomes, and must commit to adopting a “people perspective,” which includes living its positive core principles at every level of the organization.

### The role of people in an organization’s success

What we mean by a people perspective is corporate understanding that people, and *only* people, are ultimately the answer to the problems the organization faces. An organization can institute controls over processes as a hedge against human error and/or deviousness, and adhere to strict, zero-tolerance policies that punish offenders. But it’s up to people to implement the controls. It’s up to people to decide that their job is too important to risk illegally lining their pockets. Management can harp on processes and controls until blue in the face, but if its people are out of compliance, the processes won’t deliver the desired outcomes.

For example, your company may have a published protocol for dealing with sexual harassment complaints, but if the overall environment of the company is so toxic that a victim does not feel free to come forward, that “control” you’ve put in place is ineffective. Similarly, you may have a reconciliation process to prevent fraud, but if the person performing the reconciliation feels alienated from the company, he or she may simply go through the motions, so no actual reconciliation is performed and fraud against your company goes undetected.

We propose that companies modify their traditional control approach to managing deviant behavior, including fraud, to include an integrated humanistic approach. This humanistic approach requires leaders to be honest about human behavior and why business has not succeeded in keeping people in check with organizational and cultural norms. The answer lies in broadening our limited punitive control-based perspectives and appreciating the need to build organizations that invest in building better corporate citizens. In the following pages, we will introduce you to some of the philosophies that we hope to bring to the business world through our research and training in the pursuit of a more humanistic approach to solving these problems.

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<sup>1</sup> Bennet, Rebecca J. and Robinson, Sandra L. (2000). Development of a Measure of Workplace Deviance. *Journal of Applied Psychology* 85, (3), 349-360.

**Simply stated, we want to help build better organizations that enculturate better people who make better decisions while engaging in less deviant behavior, including fraud.**

To succeed at building a better organization, management cannot rely on bandages or half-measures. They must fully understand why deviant behavior such as fraud persists in business and how to implement a people-centric philosophy that encourages employees to make better decisions that drive enhanced performance in a controlled manner.

Here are some of our core ideas and questions you will want to keep in mind as we continue:

- A business is a complex living organism. Why is a positive organizational climate, which includes ethics, so imperative for an organization's overall success, including the goal of limiting deviant behavior and fraud?
- Look beyond controls and policies. Why do these mechanisms continually fail to prevent deviant behavior?
- Evaluate management's priorities. Why is deviant behavior and fraud prevention not top-of-mind for leaders?
- An ethics program, including workplace ethics training, clear expectations, and corrective action, is a cornerstone of an organization's culture. But what does a good ethics program really look like?

Whether you're a CEO, a business professional, a lawyer, a certified public accountant, an independent or in-house fraud investigator, or an ethics & compliance specialist you can only excel if you have a strong understanding of people and their behavior and how to harness common values to drive good decisions reducing the potential and impact of deviant behavior.

## CHAPTER I: Understanding Deviant Behavior

The first step toward eliminating deviant behavior is to understand why the average person might indulge in actions that could harm your organization. It could just be that the human brain is hard-wired for deviousness and corruption. Whether the literature you favor is Biblical or scientific, there is ample evidence to support that assertion. But surrendering to cynicism isn't an option when you're trying to protect your company and build a more positive corporate culture. Instead, let's take a brief look at what researchers have found regarding deviant workplace behavior.

In his book *Predictably Irrational*, Dan Ariely<sup>2</sup> explores a thought experiment designed to illustrate how easy it might be to tempt an everyday person to commit fraud. Researchers at MIT left six packs of Coca-Cola in a communal dorm building refrigerator. They also left a plate of unattended cash nearby. Guess which one vanished? If you said the Coca-Cola, you win the plate of money. One possible conclusion is that human beings look for ways to insulate ourselves from the guilt we associate with theft. Taking money has a strong connotation of stealing, whereas lifting a can of Coke from a fridge is simply "helping ourselves." Also, it's easier to rationalize taking a soda when we want a soda, rather than taking the money which we don't need to go and buy a soda.

Here's another example. You're at the office when your spouse calls. Your child needs a red pencil to complete a school assignment tomorrow. Your office keeps plenty of red pencils stocked, you are an accountant after all. So, you take one. Now suppose your office doesn't have any red pencils. Instead, you turn your attention to the cash box at the receptionist's desk, which has more than enough money to buy your child the pencils she needs. Chances are pretty good you're not going near that cash box. It's easy to rationalize the red pencil as a perk, but stealing is stealing, and that's where we draw the line. In red. With a stolen pencil. But if a pencil is a perk,

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<sup>2</sup> Ariely, Dan. *Predictably Irrational: The Hidden Forces That Shape Our Decisions*. New York City, HarperCollins, 2009.

what about information? Especially information we have labored over. Shouldn't we be entitled to use that information to our advantage in a little stock trade? Where does it all end?

One fact that becomes apparent from these examples is that human beings are capable of rationalizing bad behavior. Understanding why we give ourselves permission to rationalize can help us create a culture of countervailing forces that can bring us back into line with ethical norms. Without getting too deep into human psychology, it's worth noting that deviant behavior is often a learned response. People who have been raised without an ethical code are less likely to be ethical. People who have been betrayed feel less of a compulsion to play by the rules.

One term we often hear is confirmation bias, which refers to our likelihood to behave in accordance with our previous experiences and beliefs. Employees who have been treated poorly in life may expect to be treated poorly in the future. They may not trust peers, managers or the company, and they may take even the most constructive criticism as confirmation of their biased state of mind. They may have a tendency toward selective perception that chooses to see the negative rather than the positive. Such individuals generally do not buy into theoretical rights and wrongs, especially when the organization does not have a strong culture of ethics.

### Employees and ethical dilemmas

Deviant behavior can be seen as an ethical failure in that an ethical dilemma presented itself and the actor chose the wrong course of action. So, it is important to our understanding of deviant behavior that we recognize a simple fact: all human beings have limitations when it comes to recognizing ethical dilemmas, processing them, and committing to the most ethical course of conduct.

In research entitled, *Ethical Decision Making: An Integrated Approach*, Mark S. Schwartz<sup>3</sup> describes two traditional models for understanding the process a person goes through when faced with an ethical dilemma, which he defines as “a situation in which an individual must reflect upon competing moral standards and/or stakeholder claims in determining what is morally appropriate decision or action.” These are:

- **Rationalist based** — These models “specifically assume moral reasoning dominates the process leading to moral judgment.”
- **Non-rationalist based** — These models “assume that both intuition and emotion dominate the moral judgment process, with moral reasoning playing a secondary ‘after the fact’ explanatory...or justificatory...role....”

Schwartz notes that an understanding of a “dual-process” is emerging, “whereby there is concurrent interaction between intuition (impulsive) and reason (reflective) leading to moral judgments.” The integrated model for ethical decision making (I-EDM) Schwartz proposes contains many salient points for our discussion. First, there is the starting point at which the individual encounters a situation and either recognizes it as an ethical dilemma or does not. Without recognition, no ethical discernment can take place. However, if the individual does realize he's facing an ethical dilemma, Schwartz suggests that numerous forces are at play that impact the interpretation of the event including: reason, emotion, intuition, situational factors, and individual factors, as well as insight gained if the individual chooses to consult someone else about the dilemma.

Schwartz notes that the “personal situation,” especially if there is a “need for personal gain” can produce “ethical vulnerability.” In other words, “if one is in a weak financial position, facing significant perceived financial pressures or obligations, with few or non-existent career or job alternatives available, one would presumably be in a much weaker position to resist unethical requests and put one's job, promotion, or bonus at risk or be willing to accept the ‘personal costs’ of taking moral action.” However, there can be

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<sup>3</sup> Schwartz, Mark S. (2016). *Ethical Decision Making: An Integrated Approach*. *J. Bus. Ethics* 139, 755-776.

opposite pressures from the “norms” of the organization, “defined as those prevailing standards or expectations of behavior held by members of a particular group or community.” These prevailing standards have the potential to neutralize some people’s ethical vulnerabilities.

This brings us to the next point. Employees are not simply individuals; they are members of an organization. Therefore, full understanding of deviant behavior must include an understanding of how organizations can unwittingly incentivize, or at the least fail to discourage, deviant behavior.

### Employees as members of an organization subject to its culture

In a paper entitled *The Relationship of Ethical Climate to Deviant Workplace Behavior*,<sup>4</sup> authors Steven H. Applebaum, Kyle J. Deguire and Mathieu Lay performed “a literature review of the existing body of empirically based studies relating to the causes and implications of how the ethical climate of a company ultimately affects the incidence of workplace deviance.” In this paper, the authors identify two major categories of workplace deviant behavior: organizational deviance, which directly affects the company, and interpersonal deviance, which affects individuals within the company. Each major category has two subcategories, as follows:

- **Production deviance** — A form of organizational deviance that includes leaving work early, taking excessive breaks, intentionally working slowly, and wasting resources.
- **Property deviance** — A form of organizational deviance that includes sabotaging equipment, accepting kickbacks, lying about hours worked, and stealing from the company.
- **Political deviance** — A form of interpersonal deviance that includes showing favoritism, gossiping about coworkers, blaming coworkers, and competing nonbeneficially.
- **Personal aggression** — A form of interpersonal deviance that includes sexual harassment, verbal abuse, stealing from coworkers, and endangering coworkers.

As to the reason’s employees behave in a deviant manner, the authors suggest various contributory forces within the company, which include:

- **Presence of counter norms** — The authors observe that “organizations often reward behavior that is counter to what is generally accepted as ethical.” If a company allows employees to advance through unethical means, this “encourages employees to view ethics as an obstacle to profit.” This creates a superficial culture where “individuals ... are concerned with whether they can manage to appear ethical” rather than “relying on legitimate morals.”
- **Operational environment** — Employees are generally adaptable and “have a tendency to incline towards certain illegal activities because of socialization or other organized processes.” The authors write that “several conditions increase the likelihood that illegal activity will occur,” and note particularly that employees of “larger firms, operating in a dynamic environment possessing unlimited resources are most likely to engage in illegal behavior.” After all, if resources are unlimited, the company isn’t going to miss the little red pencil walking out the door. The authors provide an important *caveat* that “organizations and industries can exert a powerful influence on their members, even those who initially have fairly strong ethical standards.”
- **Group behaviors** — Almost everyone likes to fit in, and workers will adopt the behaviors of their peers. Here, the authors also emphasize a point related to management’s role throughout a company: “deviant role models within a group setting will significantly influence others within the group.”
- **Organizational commitment** — The authors define this term as “a state in which an employee identifies with a particular organization and its goals and wishes to maintain membership.” Thus, companies with “benevolent climates” engender organizational commitment, which discourages deviant behavior. On the other hand, companies with “egoistic climates,” where each worker is

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<sup>4</sup> Applebaum, Steven H., Deguire, Kyle J., Lay, Mathieu (2005). The Relationship of Ethical Climate to Deviant Workplace Behavior, *Corporate Governance* 3 (4), 43-55.

out for himself “were negatively related to commitment” and therefore more conducive to deviant behavior.

- **Organizational frustration and change** — Stressors and disruptions within the workplace can drive employees to think of themselves first and even act out against perceived injustice in the workplace. As Rebecca J. Bennet and Sandra L. Robinson observe in their paper, *Development of a Measure of Workplace Deviance*, frustration in the workplace “has been found to be associated with spreading rumors, vandalism, theft, aggression, and sabotage.” However, it bears mentioning that Applebaum et al. found that aggressive behavior is generally an individual problem with the aggressor and not an organizational problem.

As these categories demonstrate, the organization can give implicit permission for deviant behavior or at least tacit indifference toward preventing it. Now, would the opposite be possible? Could a company act affirmatively to create a culture that discourages deviant behavior? The answer is absolutely. Let’s explore this in more detail.

In research entitled *The Effects of Organizational and Ethical Climates on Misconduct at Work*,<sup>5</sup> Yoav Vardi looks at organizational misbehavior, which he defines as “any intentional action by members of organizations that defies and violates (a) shared organizational norms and expectations, and/or (b) core societal values, morals and standards of proper conduct.” In other words, Vardi explains, deviant behavior “is [theoretically] a product of the interaction between factors at the individual level and factors at the organizational level.” Vardi asserts that “organization culture...is one of the principal factors affecting individual motivation and behavior in general and misconduct in particular.”

Vardi defines culture as “a system of shared values which produces normative pressures on members of organizations.” But how does a system come about? Vardi explains that “[b]y communicating expectations and by role modeling, managers transmit these cultural precepts to members, not only in regard to desirable and acceptable behavior, but also in regard to misbehavior.” If this communication is unclear, inconsistent, or contradictory, the result is “a weak culture, [where] the values, goals, purposes, and beliefs of the total organization are not clear and therefore diverse subcultures are likely to emerge. Members’ behaviors then are likely to rely on norms generated by their referent groups or relevant subcultures.”

In other words, if management does not send a clear, unequivocal message about what the organization as a whole stands for, different departments, working teams, and social cliques will fill the void with their own ethical values. This can create a situation where the “climate” varies throughout the organization. Vardi writes that climate “expresses those perceptions shared by organization members that reflect the way they comprehend and describe their organizational environment.” This can produce a strong counter signal about “what management says” versus “the way things are around here.”

On the other hand, organizations can have a strong “ethical climate” that “reflect(s) common perceptions and beliefs concerning organizational expectations of proper conduct.” Vardi’s research found that “the more positively organizational climate is viewed, the less the reported misbehavior in the organization.” So, it might just be possible for an organization to exert a countervailing force that would bring wayward employees back into line with ethical norms. The question is, “Do businesses do this?” Unfortunately, the answer is “Not very effectively.”

### Deviant behavior and employer blind spots

To understand why businesses are not generally successful in reducing or eliminating deviant behavior, we have to appreciate some of the blind spots employers have toward the topic. Take as an example this internal fraud scenario. A business owner is distressed because even though his revenues are consistent, he can’t seem to find money to pay the utility bills. He asks a forensic investigator to come in and look at the books and tell him where the problem lies. The conversation might go something like this:

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<sup>5</sup> Vardi, Yoav, *The Effects of Organizational and Ethical Climates on Misconduct at Work* (2001) *Journal of Business Ethics* 29, 325-337.



“I don’t understand. We’ve been doing really well and nothing has changed businesswise — we just don’t have any money. Can you help me figure it out?”

Any fraud investigator worth the fee will know which question to ask first:

“Whom do you trust the most?”

“Well, Betty, of course. But she’s a 30-year veteran of the company, totally loyal. I hired her myself! She would never steal a dime.”

But, of course, the reason for the cash shortfall is “Betty.”

What follows is a lot of surprise and indignation, which only goes to prove that employers suffer from selective perception and confirmation bias as well. It’s unfortunate that this business owner couldn’t recognize the obvious: the person with the greatest knowledge of how the company operates and the highest degree of trust had the opportunity. That’s because trust goes hand in hand with access and fraud occurs when people have access to value.

This brings up another point about fraud, as a particular type of workplace deviant behavior. Fraudsters need to be trusted. By definition, it is their abuse of the trusting relationship that enables them to unjustly benefit. On the other hand, for a business to get anything done, leaders must trust their people. Trust, but verify.

Here is another example where an employer blind spot prevented him from seeing the red flags. Let’s imagine you have a bookkeeper, manager, process owner or somebody similar who seems to always need to be there, on-site, checking on things. It looks like benign and commendable behavior — the “organizational commitment” Applebaum et al. described — until you realize the real reason they never leave they want to be there to make sure their scheme isn’t uncovered by some curious party. Consequently, they appear to be extremely dedicated and willing to always “help out.”

Returning to Betty for just a moment, recall that she had knowledge and opportunity. And, if the employer had taken the time to know what was going on in Betty’s life outside of work, he might have discovered there was motive. Given what we’ve said earlier about individual inducements towards deviant behavior, an employer cannot be blind to these factors affecting workers:

- Financial distress
- Drug addiction
- Spouse’s loss of employment
- Family illness
- Job dissatisfaction
- Issues with organizational culture, including frequent conflict with bosses or colleagues
- A lack of, or a perceived lack of, recognition at work
- Perceived nepotism or favoritism toward “rival” employees
- Anticipated but unfulfilled psychological rewards

Weirdly enough, that last one, psychological rewards, dovetails with modern technology in a surprising way. Anticipated psychological rewards are a new addition to the traditional motivators we come across for committing fraud. A psychological reward can flow from a positive accomplishment, such as achieving recognition for a quality presentation. But the flip side can be the rush that comes from feeling superior, fleecing others, or otherwise executing a well-honed skill to somebody else’s detriment. Think of somebody a little less than heroic, but whom we seem to universally respect anyway, like Walter White (Breaking Bad) and Don Draper (Mad Men). The thrill for them had to do with exercising either expertise or power over others. The thrill of being rich was a distant second place.

So how can you recognize ethical issues in business before they become big problems? By training yourself to look for red flags the way our ancestors trained themselves to watch for sleeping snakes in tall grasses. Want to really remove your blinders? Take a hard look at your company HR statistics — including the type, severity and consistency of on-file complaints. These are a treasure trove when it comes to understanding the ethical culture you want and the actual climate in which your employees operate. So is turnover. Your organization shouldn't be churning through employees like a riverboat. If that's happening, it's probably because your company's sense of its ethical culture is ill-defined or in conflict with reality.

## Chapter II: Why the Traditional Response to Deviant Behavior Doesn't Work

Businesses that fail to spot deviant behavior early on risk greater losses as the situation festers or the fraud escalates. But, when the evidence finally flashes bold enough to pierce the darkest veil, the employer must respond. Now, you think, at last, the problem will be solved, but we're afraid that's much too optimistic. The company may resolve the single incident it uncovers, but if the approach is a traditional one, the conditions which allowed the deviant behavior to occur will remain, so any victory will likely be short-lived.

The problem is that the traditional approach to managing deviant behavior is merely punitive. This means the stick, rather than the carrot. The message traditional companies send to employees, a good one at first blush, is that operating with integrity is safer and more beneficial than behaving poorly. Toe the line, workers are told, and you get stable employment with such and such benefits. Step out of line, and you face disciplinary sanctions, up to and including termination. It is a system that encourages rational, far-sighted workers to keep their noses to the grindstone and to walk the straight and narrow.

But there are at least a couple of very important reasons why the punitive approach is not very effective. As Schwartz explains, employees don't always pause to perform the risk-reward calculus, especially when they are under emotional pressure that prevents them from thinking rationally. So, it is not an effective deterrent. Moreover, punishment does little to prevent repeat offenses, because employees with confirmation bias are likely to see punishment as further evidence of injustice towards them, and that feeling that they are laboring within an unjust system may feed job frustration that drives them to act out in some way to get even.

The punitive approach also fails because it only accounts for half of human motivation, the fear of punishment, while ignoring the other more powerful motivator, the promise of reward. Rewards can include advancement within the company, salary increases or bonuses, recognition among peers, or praise for work well done. A just reward system encourages our aspirations, which brings out the best in us. Thus, simply put, the traditional, punitive approach does not work because it ignores our better nature.

Organizational management must understand it is not feasible to threaten your way into a more ethical company culture. People respond poorly to coercion, so when you attempt to enforce good behavior with a narrow focus on unwelcome behaviors and their respective punishments, you miss the opportunities to be gained by living, demonstrating and promoting the benefits of the positive behaviors.

### If not a punitive approach, then what?

We have now established that people are key to your organization's success, but that people who engage in deviant workplace behavior can also be your undoing. It is imperative to eliminate or at least reduce deviant behavior among your employees, but a singular focus on punitive measures is not going to succeed. So, if the stick alone does not work, is there an effective carrot? And what would such a carrot look like?

### Should organizations pay people to be ethical?

The answer to this question probably isn't as straightforward as you'd like to think. It's true that ethical behavior needs to be linked to performance — and, ultimately, to a company's appraisal system and compensation. So, yes: there is at least a semi-formal incentive program urging your employees to demonstrate your organization's core values.

But when was the last time your organization reviewed its job descriptions? Do your job descriptions set forth the expectation that your associates live the organization's core values? We encourage everyone to look at your job descriptions and see if this critical component is included. While you are at it, make sure that the descriptions accurately reflect what people are doing. A simple question to ponder: If your job descriptions are not up to date, how do people know what they are to do? Furthermore, how can you have an effective performance evaluation system without accurate job descriptions? You really can't.

Yet, any incentive program is going to sputter and stall if you are not hiring people who share the organization's values. Remember our mention of cultures where employees feel it's enough to put on the appearance of being ethical? An incentive program that encourages folks to put on a show for you is not delivering what you're paying for.

From that perspective, it really is not appropriate to "pay" for someone to behave ethically if ethical behavior is not in their wheelhouse, and does not feature prominently in their collective experiences, to begin with. To take a prominent example, one might think that paying a CEO several thousand times the rate of your average employee would encourage rational behavior from a presumably intelligent person who would not want to kill the golden goose. Not so, apparently. We can point to [any number of fairly recent papers](#)<sup>6</sup> (e.g. "Throwing Caution to the Wind: The Effect of CEO Stock Option Pay on the Incidence of Product Safety Problems" from the July 2015 issue of *Strategic Management Journal*<sup>7</sup> and Peng and Röell's "Executive Pay and Shareholder Litigation" from *Review of Finance* in 2008<sup>8</sup>) that reveal a disappointing truth about CEO compensation: those who are compensated with stock options — which become more valuable as the company succeeds — tend to preside over more product recalls and shareholder lawsuits than CEOs who are not compensated with stock options. Other research throughout the years seems to corroborate the idea that the world's most well-compensated chief executive officers [tend to perform more poorly](#)<sup>9</sup> than CEOs with more average salaries.

So, if you can pay a CEO many millions of dollars a year but *still* can't expect them to behave in a consistent and ethical manner, you have no hope at all of inspiring greatness in the employee who takes home minimum wage. That is, not if you're expecting money alone to do the heavy lifting. In this context, money is a middleman you can't afford.

### Chapter III: Developing an Incentive Program that Works to Promote Ethical Behavior

While the types and amounts of compensation doled out under your roof no doubt vary with the nature of the work being done, your goal should be to instill consistently ethical behavior throughout your organization. It shouldn't *matter* if your CEO is paid in stock options or soybeans. Compensation should be an expression of something more than pure monetary value — it must be an expression of *human* values, too.

Here are two questions to consider if you intend to build an incentive program that organically links the process of being *compensated* with the process of *behaving ethically*:

1. What does "going above and beyond" look like in your organization?
2. How does your communication and reward program sustain your definition of excellence?

Drawing on the research we have previously discussed, we envision a process that hires the right people, invites them to participate in an ethical business culture, and gives them the tools and support to make

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<sup>6</sup> Sebenius, Alyza, "CEOs Behaving Badly: What a chief executive's golf game and handwriting say about his compensation—and his leadership." *The Atlantic*, April, 2016.

<sup>7</sup> Wowak et al., (2015) Throwing Caution to the Wind: The Effect of CEO Stock Option Pay on the Incidence of Product Safety Problems. *Strategic Management Journal*.

<sup>8</sup> Peng and Röell (2008). Executive Pay and Shareholder Litigation. *Review of Finance* 12 (1), 141–184.

<sup>9</sup> Adams, Susan. "The Highest-Paid CEOs Are the Worst Performers, New Study Says." *Forbes.com*, June 16, 2014, 09:59am, <https://www.forbes.com/sites/susanadams/2014/06/16/the-highest-paid-ceos-are-the-worst-performers-new-study-says/#27568e4a7e32>

ethical decisions for their good and the good of the organization. Those tools and support come from a robust ethics program. Research we have cited, as well as additional sources, have proposed a wide range of benefits arising from a structured ethics program, including:

- Greater employee satisfaction and job engagement
- Lower employee turnover
- Improved employee productivity
- Fewer available rationalizations for fraud
- Attract and retain the best talent in your industry
- Happier and more satisfied customers
- Better and wider recognition as a company that “does the right thing”
- Employees are willing to “blow the whistle” when seeing inappropriate behavior

A leading global communications marketing firm called Edelman performs annual studies of trust as it applies to the world of commerce, business, and supply-and-demand. Efforts like these shed some light on where the public stands — or, more accurately, where it wishes to stand — on the subject of trust as it applies to business, personal and civic life. Consider [their findings](#)<sup>10</sup>:

- 49 percent of consumers, globally, trust public institutions like government
- Between 50 and 60 percent of consumers trust businesses
- 91 percent of consumers indicated purchasing a product or service recently because they trusted that company
- 77 percent of consumers refused to purchase a product or service recently from a company because they did not trust that company

These data clearly suggest a healthy level of consumer skepticism towards public and private entities and indicates that a company’s reputation seriously influences consumers’ buying patterns. Therefore, trust is a business asset. Moreover, we know from our own experiences that consumer trust is not merely a response to a product’s prior performance. All companies have frontline employees who may not sit in board rooms but are the public face of the company for the consumers with whom they interact. Positive exchanges between your employees and the public matter to your bottom line. These depend on the quality of your employees, who are greatly influenced by the environment in which they operate.

The optimal environment for employees is one that offers rewards, both tangible and intangible, for excelling at their jobs and making sound, ethical decisions. But this environment, which we can call corporate culture, doesn’t appear randomly out of thin air. It results from deliberate planning and dedicated socialization of core values throughout the organization.

As was mentioned in the opening, you cannot build an ethical organizational culture on half-measures. What we are calling for is a re-imagining of the Human Resources Department to become a more active participant in organizational ethics programs that teaches business ethics and reinforces those teachings — with the active participation of management — at every level of your organization. Before we explain how this might work, we have to address a common objection about the teaching of business ethics.

### Can business ethics be taught on an organizational level?

As the great educator, Horace Mann said, “Manners easily and rapidly mature into morals.” This might give us hope that by laying down a few rules of politeness— what businesses call their Code of Conduct — and modeling those rules, management can encourage individuals within an organization to become moral, ethical members of that organization. But, while hope springs eternal, Horace Mann also said, “A human being is not, in any proper sense, a human being till he is educated,” and that is the discouraging rub. We cannot expect individuals who have not gone through any ethical formation to behave in an ethical manner, and sadly, ethics are not being taught effectively, if at all, at any level of our educational system. That means workers come to employment without any formal training in ethics. And yet,

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<sup>10</sup> Edelman Trust Barometer <sup>TM</sup> <https://www.edelman.com/research/edelman-trust-barometer-archive>.

companies take for granted that workers will observe the Code of Conduct because they are innately good people or, at the very least, because they fear the stick of discipline. Is it any wonder we have a problem with deviant workplace behavior?

Clearly, there is a need for ethical training. But often management will object on the basis of it “not being our job,” or “being too intrusive on workers’ privacy,” or “taking up too much of company time.” Let’s address each of these objections in turn, starting with “not our job.”

Here, the old adage, “If not us who? If not now when?” comes to mind. If your organization is onboarding employees with dubious ethical training, and you understand how this poses a risk to your organization, how do you propose to address the risk? You know that simply handing them an employee handbook with rules for conduct on page 23 is not going to make an impression. So, failing to take proactive steps to inculcate ethics is sheer negligence.

As for intruding on the workers’ privacy, it’s clear we are not our brother’s keeper, and an employee’s private morals are not the company’s business. Management should not interest itself in its employees’ personal lives nor demand conformity with “right thinking.” But when it comes to public conduct and whether, for example, it’s permissible to raise your hand to another worker or falsely take credit for someone else’s ideas, the company can and should speak clearly.

Finally, the notion that ethics training takes too much time away from job-related tasks is extremely short-sighted. When you weigh the costs of ethics training against the losses due to fraud or liability for a sexual harassment lawsuit or some other consequence of deviant behavior, it’s clear that ethics training is a sound investment.

Many companies who have expertly drafted Codes of Conduct suffer egregiously from deviant behavior, because they do not support the implementation of their code with sufficient training. Putting the onus on the employee to comply with a Code without training is doomed to fail, because most of us humans fall woefully short in our attempts at self-examination and self-correction. Take, for example, any number of polls that show how [vastly Americans overestimate how well-informed we are](#).<sup>11</sup> A random sampling of Americans would turn up very few who would admit to being actively “unethical,” but nevertheless, we all have blind spots about how stellar our leadership is or how well-behaved we are when no one is watching. So, if we are all generally poor judges of our own character, we can all benefit from a robust corporate ethics program which provides a rubric against which to judge behavior which would otherwise occur in a private little vacuum.

A distinct advantage to studying ethics in a collaborative and structured way is that it gets us “out of our own heads” for a little bit, so that we actually place ourselves, our behavior, and our preconceptions in a context with the rest of humanity. To put it another way, “practicing” and “teaching” ethics is a way of refining our personal morals in conformation with shared ethical values which can be practiced in institutions, businesses and governments. So, yes, ethics can and must be taught on the organizational level. But what would a solid organizational ethics program look like?

#### Chapter IV: The Four Core Components of a Robust Organizational Ethics Program

There are four core components to a successful ethics program that addresses and reduces deviant behavior in the workplace:

- **Values** you have identified that truly and accurately reflect what your organization stands for
- A **Code of Ethics** that articulates the values of the organization, has the full support of management from top to bottom, and resonates with employees at every level

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<sup>11</sup> Avirgan, Jody, “Americans Feel Well-Informed, Which May Be The Problem.” Five Thirty Eight, Oct. 7, 2016, 1:30 PM, <https://fivethirtyeight.com/features/americans-feel-well-informed-which-may-be-the-problem/>

- **Empowered stakeholders** who uphold the organization’s values by hiring and promoting the right people, training and assessing employees in ethics, and exhibiting leadership in accordance with the organization’s Code of Ethics
- **Communication** which clearly and consistently articulates, applies and reinforces the organization’s values during day-to-day operations

These four core principles work synergistically to create an ethical culture that permeates the organization providing incentives for positive behavior and disincentives for deviant behavior. We shall discuss each core component in turn.

### Identifying Values

What does your company stand for? Profits or perhaps having a positive impact on your constituents in the case of a charitable organization. But by what means and methods? The beauty of capitalism is that it is based on a system of voluntary exchanges. You can’t force customers to buy from you, so you have to please them. You can’t force talented employees to work for you, so you must offer them a rewarding experience. When a company focuses on those two broad goals — customer and employee satisfaction — it’s on its way to developing an ethical culture. Why? Because caring about others is a bedrock ethical concept.

Moreover, these two concepts go hand in hand. You want to please your customers by offering a superior product. You want to give your employees the opportunity to grow professionally by constantly improving your products and services. Each goal advances the other.

So, what are some values your company might embrace? On the customer side, you might select excellence, innovation, economy, luxury, availability, responsiveness, courtesy, and anticipating needs. For your employees, you might focus on productivity, opportunity, recognition, honesty, diligence, responsibility, initiative, creative problem solving, collegiality, leadership, and skill development. You can also develop a list of values for your products or services.

Finally, the company must embody the values it articulates. There’s no sense demanding your workforce be honest if you’re dumping toxins into the local reservoir. Good corporate citizenship, demonstrated through regulatory compliance and charitable endeavors, can go a long way in promoting an ethical culture. Above all, the values selected must ring true, if not in present application, then at least as worthy aspirations.

### Building a Code of Ethics

Your organization’s Code of Ethics is a statement to everyone about the values you hold and the professional, ethical way you conduct business. It is a recitation of the values you uphold, such your “passion for the customer,” your commitment to “selecting and empowering the best employees” and “providing the opportunity for a rewarding career,” your dedication to being “good corporate citizens and good neighbors.” Your Code may also list deviations from those values that you will not tolerate. But your Code is also how you tell the world *outside* your walls what you value, so it’s useful as a public relations tool, but only to the extent that you can demonstrate to outsiders your commitment to your Code.

In today’s culture, making any definitive statement about what is “right and wrong” is a bold proposition. But as Vergil tells us, “Fortune favors the bold.” If you do not speak unequivocally about what behavior is acceptable, employee interpretations of “what goes around here” will proliferate. The last thing you want to deal with is an endless lineup of offenders crying, “How was I supposed to know I wasn’t supposed to...?” So, be bold.

If your organization doesn’t have a Code, you’ll have to start from scratch. If you have an existing Code, it’s likely that no one in your company has referred to it in a while. So, take it out, dust it off, and see if portions should be revised according to your recent experiences with deviant workplace behavior or where you perceive the risks might be. You may want to take a start-from-scratch approach as well.

As a first step, you can take a look at the competition. It's common for companies to post their Codes of Conduct on their websites, and, in fact, certain companies are required to do so. What do you like about their Codes? Do they express values your organization also upholds?

According to the business website *i-sight.com*<sup>12</sup>, "A great code of conduct is:

- **Written for the reader.** It is easy to understand and doesn't include any technical or legal jargon.
- **Comprehensive.** It covers all important details that may impact the daily lives of employees and answers common questions that arise.
- **Supported by leadership.** It has been acknowledged and approved by the company's senior management team. This is often demonstrated in the form of a foreword written by the CEO or President.
- **Accessible.** It is available to all employees, current investors and potential investors.
- **Visually appealing.** It follows a style that is clean and reflective of the organization."

We looked at a few corporate Codes of Conduct and found these recurring elements:

- Summary statement of the company's values
- Employees' responsibility to uphold the company Code by acting ethically and reporting ethical violations
- Employees' responsibility to demonstrate respect for the company and individual workers
- Employees' right to speak up without fear of retaliation
- Company resources available to assist employees who have ethical concerns
- Employees' right to work in an environment free from harassment and discrimination
- Employees' right to work in a safe environment, along with the responsibility to speak up about safety concerns
- Company substance abuse policy
- Company commitment to product excellence
- Company commitment to honoring privacy
- Rules for engaging with suppliers, vendors, and contractors
- Rules regarding common ethical and legal violations, such as offering or accepting bribes, giving or accepting gifts, or engaging in insider trading
- Clear statements on identifying conflicts of interest and the process for dealing with them
- Clear statement on the value of fair competition in the marketplace and tactics that are not allowed
- Clear statement on the importance of accurate recording keeping and observing processes and controls
- Clear statement on the importance of acting in compliance with state, federal and local regulations
- Clear statement on the importance of preserving company assets and the consequences of theft or vandalism
- Clear statement on the importance of preserving the company's trade secrets and proprietary information
- Rules for sharing information about the company or speaking on behalf of the company

You can probably think of some other points that are specific to your organization. As you assess your existing Code or consider formulating one, here are some questions to consider:

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<sup>12</sup> Munim, Adil "18 of the Best Code of Conduct Examples", *i-sight.com*, <https://i-sight.com/resources/18-of-the-best-code-of-conduct-examples/>

- Are your policies written in plain language that is easy to understand? Do they anticipate common follow-up questions?
- Does the Code provide for or require annual training on matters related to ethics and conduct?
- Is the Code clear about what constitutes a “conflict of interest” — even if it’s merely the *appearance* of such?
- Does your Code of Ethics include rules for social media?
- Does your Code allow the organization to conduct background checks — even after the hiring process is complete?
- Is your Code of Conduct uniform? Does it apply in equal measure to employees and to upper leadership?
- Does your Code of Conduct establish accountability and “ownership” over processes — most particularly the processes related to deviant behavior and fraud?
- Does your Code include a way for people to report violations and explain that retaliation will not be tolerated for bringing a good faith concern to light?

Whether you are revising an existing Code or drafting an initial version, you should consider the process that produces a Code. Will yours be the work of one individual or a representative committee? Remember that you’re not turning out a static document that a new employee might leaf through lazily once in their first afternoon and not think of again. Nor should it be fodder for PowerPoint orientation lectures. Your Code must be integral to your organization, so it should be created via a process that gets the most buy-in from management and rank-and-file workers.

Once you have a Code of Ethics, you have a cornerstone for your Ethics Program. It’s time to bring that program to life.

### Engaging HR to advance your company ethics program

Up to now, we’ve been talking a great deal about the importance of people to your organization and, thus, the importance of a people-centric approach to organizational issues. So, where do you currently go when you have a people issue you need to resolve? Your Human Resources Department has that general responsibility and, presumably, the expertise to assist. This makes HR a logical partner for the development and implementation of a company-wide ethics program, especially for companies that are not large enough to hire a dedicated Ethics Officer.

There are a number of ways HR can assist in this endeavor. First, as we have discussed, you gain some protection against deviant behavior by hiring and promoting people who share positive values and already have well-formed ethics. Certain shared notions — that it is wrong to lie, to steal, and to touch a coworker inappropriately — help establish a respectful and functional workplace. On this issue, your Human Resources Department is your first line of defense. HR is tasked with providing hiring managers with the tools they need to make the right staffing decisions. These tools can include interview questions that are infused with simple ethical dilemmas, such as this:

“A fellow employee tells you that he only does about one or two hours of “actual work” on the two days he’s allowed to work from home in a given week. Do you follow suit?” There’s only one right answer here, of course — and not just because there’s a potential job on the line. But how an applicant answers and how long it takes them to do so can tell you a lot about how their “moral mind” works.

Since HR is involved in the hiring and promotion processes, it should be empowered to screen for lapses in character that could make for a bad hire or promotion and to set expectations for proper behavior once an employee is hired or advanced.

In other words, HR must work closely with management to onboard ethical people, instill in them the importance of behaving ethically while they are with the company, and enforce the Code of Ethics during employment. This can mean conducting social media searches and background checks. Too often prospective hires have posted statements that would hold the company in a negative light. Also, it’s very common for companies to forego a background check or even phoning references, when they think they’ve



landed a solid prospect. Unfortunately, too often, they regret cutting those corners when problems surface. Diligence at the hiring process that screens out “bad apples” is essential for limiting deviant behavior.

This brings us to a second crucial point. Management and HR must have a close working relationship focused on shared goals and objectives. Too often management sees HR as an impediment or an adversary in the hiring and performance review processes. HR can feel unsupported in its efforts and may be less likely to raise issues with management if doing so is not worth the grief. That’s when communications break down and management does not get the information it needs to make the best hiring and promotion decisions.

Furthermore, as we’ve seen, even average-to-good people are susceptible to rationalizing deviant behavior. Therefore, when an organization brings employees aboard, it must take steps to support their ethical inclinations. The organization must treat them properly, creating an environment in which they want to belong and grow. As the function that oversees orientation, fields complaints and manages benefits, HR also has an important role to play in making employees feel valued. But ultimately the onus falls on management, especially a worker’s immediate supervisor, who must deliver a message consistent with the values enunciated during the onboarding process.

A key area where HR can act affirmatively to improve employee morale is in performance evaluations. For workers, these reviews can be sources of strife in the workplace, but HR can do a great deal to improve the process from a people perspective and increase the sense of fair play in the organization. Imagine for a moment how you would feel if someone else was credited with your work, so that you were not only overlooked at the time, but you didn’t get credit during your performance review! Was that intentional favoritism? Often, misunderstandings occur because of something as banal as an out-of-date job description, which results in responsibilities and accolades being shared inequitably.

Perceived snubs can erode an organization’s culture, but vague, inaccurate and out-of-date job descriptions can also undercut productivity. After all, how can you expect an employee to work diligently day in and day out if they don’t even have a clear idea of their duties? And how can you really hope to evaluate their performance with the fairness they expect and deserve? These conditions breed discontent that leads to disengagement, which can lead to fraud, theft, and even worse forms of deviant behavior.

Therefore, it’s important to have your HR department bring all relevant performance evaluation materials up to date. But prudent management should also want HR to emphasize the importance of performance evaluations throughout the entire organization. Returning to the idea of management working closely with HR, management at all levels should assist HR by reviewing and updating job descriptions regularly and asking employees to review the documents and attest to their accuracy.

It is our considered opinion that a company that separates normal HR functions from company ethics does so at its own peril. Unfortunately, most companies do not fully invest in HR’s potential for building a positive corporate culture. In many organizations, HR is limited to managing paperwork related to onboarding and separating employees, and in between those two events, it manages complaints. HR could perform vitally important functions related to building and maintaining a positive corporate culture, such as overseeing a structured ethics program, and management should consider the importance of having HR sponsor initiatives that drive success in this area.

### What does an ongoing ethics program look like?

Once you have finalized your Code of Ethics and partnered with HR to enhance your ethics program, what does it mean to have an ongoing Ethics Program? There are three key components: ethics training for employees, ethical training and guidelines for leaders, and aids for managing ethics in the workplace. Let’s tackle each of these in turn.

#### Ethics training for employees

You’ll recall we mentioned that ethics are not being taught effectively throughout our educational system. But the good news is that the void has created a hunger, especially within the younger generation of

workers, for exactly the type of moral and ethical formation we are talking about. Something we are seeing with millennials is that they want to work for companies with high moral standards. They're already considering, on their own, things like organizational culture and "tone at the top" as a natural part of determining whether they want to apply for a particular job or whether they will accept that job if it's offered to them. They want their jobs to provide more than the means for them to survive and pay bills; they crave something of social value, too. Something they can contribute.

And their contributions — to company morale and the company image — should not be underestimated. It's important to note that the most visible part of your company isn't your leadership, but rather the folks manning your call centers and seeing to customer problems and deliveries. The people who actually deal with your clients, suppliers, and distributors are the public face of your company. Decisions might come from the top, but the people in the middle and the bottom actually execute on that vision. If your rank-and-file employees are not living your values, the public will know it.

Therefore, regularly scheduled online training, seminars, and workshops on ethics, ethical decision making, and other topics can help employees with self-improvement, while making them feel like they belong to an organization that "walks the walk." They will have less anxiety about performance reviews, because they will feel they are working within a fair environment. Additionally, employees who feel they work in a fair and just environment will be more likely to speak up if they do see an issue. They are more invested in the organization and its success and might actually take it personally if they see somebody abusing trust or stealing something from an organization they've become emotionally and personally invested in.

### Ethics training for leaders

Do your leaders exemplify your values or just pay them lip service? This is a vitally important question for your organization to address, because your leaders set the tone for your organization. And by leaders, we don't simply mean the upper echelons of management who don't have daily or perhaps even semi-annual contact with rank-and-file workers. They may set "the tone at the top," but that tone may not permeate the deeper layers of the organization. What we mean by leaders is anyone who is in a direct position of authority over subordinate workers. Their commitment to your Code — as modeled in their behavior more than written or spoken words — will have a more profound impact on your company culture than any other factor.

Recall what Applebaum *et al.* said about the presence of counter norms. Leaders who set negative examples can easily undermine everything you hope to achieve in building an ethical culture. But there are also leaders who simply do not project your values. They're neutral figures who do not inspire or edify their subordinates. These leaders (in name only) can produce a kind of culture drought in the middle of your organization, leading to a disconnect that allows subcultures to flourish opening the door for deviant behavior including fraud. This situation frequently happens when decision-making takes place inside an organizational bubble and when you expect company culture to trickle down instead of groundswell from the bottom and the middle.

This is why it is critically important to link ethics to your organization's performance system and promotions. This is a critical component to your culture. If someone is not emulating the organization's core values, it shouldn't matter how good an operator they are — there should not be a future for them in the organization. Promoting these individuals sends the wrong message and will sour the tone and, again, add to potential justifications for others to adopt deviant behaviors.

The gap between the "tone at the top" and the "culture in the middle" is where ethics programs live. It's also where honest reflection happens. To that end, spend some time surveying your employees to help determine if you have a cultural disconnect that may result in deviant behavior. It might also point out the need to uplift and edify your middle management through leadership training that reflects your organization's values. This training should also come with the expectation that ethics is part of the performance evaluation process by which a manager's leadership is judged.

## Changing the way you communicate to build an ethical culture

Now we turn to what is perhaps the greatest challenge: communication. It's a challenge because, when the goal is to build an ethical culture, every written, oral or visual communication within the organization and from the organization to the outside world must reflect its core values. That's a tall order, and let's face it, not all of us are naturally gifted communicators.

The first step to enhancing communications, of course, is to recognize the need to change. Being conscious of the need to speak in terms of our values can bring about organic change. Suddenly we're speaking more positively, appealing to our employees' aspirations rather than to their fears. Depending on the size of your organization, you might want to contract with a communications firm or hire a professional or a team to be your Communications Department. If you have an existing department, take a hard look at its performance. Has their output contributed to a positive ethical culture? Or has it added to the disconnect and the dissonance you may be experiencing?

It's also vitally important to remember that communication is a two-way street. The old adage that "God gave us two ears and one mouth, and we should use them in that proportion" is applicable here. Management must be willing to listen to rank-and-file to get a sense of the reality permeating the organization. But worker feedback is only reliable when they feel the freedom to speak without reprisals. This brings us back to the point about living your Code. Your Code must contain statements about the value of employees coming forward with their concerns, but it must also provide specifics about the process for doing so, and the employees fielding those concerns should greet that feedback in an encouraging fashion. This requires training, which brings us back to the first component of the Ethics Program.

## Incentives for an ethics program from the Federal Sentencing Guidelines for Organizations

Organizations are generally slow to change, especially when change requires an initial investment. Even if leadership grasps the importance of changing the corporate culture, an ethics program can be a tough sell. But, if creating an environment that adds to your bottom line isn't enough of an incentive, assistance may be available from an unlikely source: the U.S. government. Yes, the government will help sell the proposition by qualifying your company for reduced fines and penalties if your business is ever implicated in certain wrongdoing. The Federal Sentencing Guidelines for Organizations grants a reduction in fines and penalties to companies that demonstrate they possess the key characteristics of an ethical culture and compliance program in accordance with Chapter 8 of the Guidelines. That little insurance policy may be just the incentive the Board of your company needs to greenlight the funding of an ethics program.

## Conclusion: Fraud's Chain of Custody

There you have it. A crash course in defeating deviant behavior and fraud by taking a people perspective. So, what are the key takeaways from this discussion?

People come to organizations with different backgrounds and experiences, which have informed their personal morals and ethics. Some will never make the cut, ethically speaking, and should not be brought on board. Others are potentially positive employees and will adapt to the organization's culture. A strong ethical culture that articulates values clearly, models those values consistently, and communicates openly empowers its employees to behave ethically to their benefit and that of the organization. A weak culture opens the door to deviant behavior, including fraud, that undermines the organization's success. Thus, fraud has a chain of custody, and we each have a role to play in its commission or prevention.

If you see the truth in all this and would like to commit to changing your organization's culture, North American Forensic Accounting is ready to help.

North American Forensic Accounting is about more than just managing deviant behavior in the workplace. We are a collaborative learning platform for executives, managers, HR professionals, ethics & compliance practitioners, lawyers, accountants, internal auditors, PR specialists, fraud investigators and anybody else who wants to establish strong cultural and ethical values in their organization. It is our goal to provide tools and thinking that help organizations improve and play a positive role in shaping better

corporate citizens. We hope you'll grow with us as we build a rich catalog of educational materials for you to study and learn from at your own pace. To do that, we've tapped some of the world's finest thought leaders on ethics, compliance, antifraud programs and controls, and leadership and will continue to seek out meaningful partnerships.

Whether you are interested in the finer details of building your company's ethics program, or you want to pursue a more structured education towards antifraud certification, consider us a resource and visit us frequently.

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