Surfing the Ethical Behavior Wave in Business

Minimize risk and maximize business outcomes

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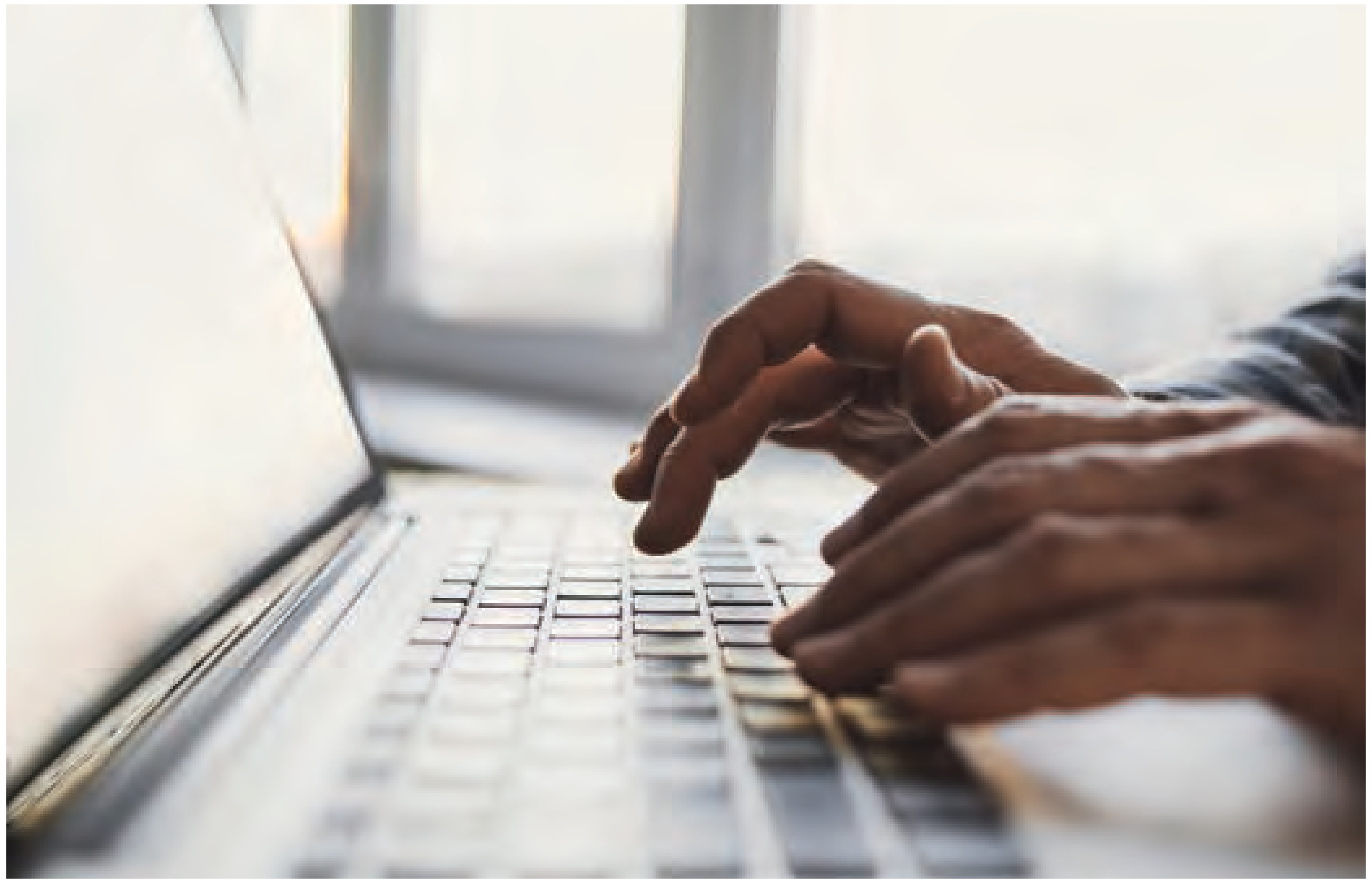
Gallagher

Key Insights

1. Broad shifts in business culture and wider societal norms are generating new challenges and risks for businesses.
2. Companies are facing the challenge of positioning themselves optimally in terms of their values and maintaining their reputation.
3. A company's ethical stance can be a key determinant of stockholder investment decisions.
4. New generations of employees are looking to align their personal values with those of the company they work for, altering hiring dynamics and intensifying competition for talented individuals.
5. Companies can mitigate vulnerability to operational and reputational risk by ensuring that the ethical component of their company culture is well-defined and consistently implemented.



Introduction

Companies today have no choice but to recognize that image and reputation are vital to sustainable success. Increasingly, stakeholders and shareholders are recognizing the value of ethical behavior, and the impact of these practices on a company's reputation and how people choose to do business with it.

Indeed, the need for an authentically ethical culture stems from a powerful wave of change that is not going to ebb any time soon. As Tom Tropp, Global Chief Ethics Officer at Gallagher, observes, "People are starting to question what companies are doing for the world and its inhabitants. I believe it's crucial for companies to publicly demonstrate what they stand for."

Amid a deluge of new norms and new risks, companies are striving for clarity on how ethics and culture sit in this matrix of shifting influences.

In a world of public, rapidly distributed scrutiny, the need to be viewed as operating ethically is more important than ever.

A constant churn of challenges

Myriad cultural and moral values are in play and sometimes in conflict within the global marketplace. In a world where citizen journalism has created infinite networks of information-sharing and potential exposure, it is increasingly challenging for companies to control the narrative around their reputation.

What drives ethical behavior in business?

In the context of reputation management, the shifting role of ethics in business stems from a variety of sources:

- Investors and shareholders are measuring company performance against environmental, social, and corporate governance (ESG) indexes, as well as against the quarterly balance sheet.
- Employees, clients, and other stakeholders, such as wider society, are scrutinizing companies in terms of diversity, equity, and inclusion (DEI) commitments.
- Customers wishing to consume ethically are influenced by strong corporate social responsibility (CSR) indicators.

Bringing ethical behavior to the forefront

What is an ethical company?

Ethics are moral principles that determine what is right (ethical) and wrong. The general perception is that an "ethical" company is one that puts stakeholder interests — those of employees, customers, community, the environment, and society — above or on par with shareholder interests. This view is, of course, subjective and very much based on an individual's own ethical code — their own decision-making framework.

As Tropp points out, "If you ask a company whether it's ethical, the answer will likely be 'yes'. However, the next step should be to ask for a definition of what its ethics are."

"When we at Gallagher talk about doing business ethically, we mean conducting business in alignment with our beliefs, values, and culture… what we call The Gallagher Way — doing what's right by our clients, communities, and our people. Our ethics are unique to us. By stating this, we open the door for people to consider whether their own values align with ours."

The Gallagher Way is pivotal to the way Gallagher does business. And, as affirmed on the Gallagher website: These shared values built us. They guide us. They inspire us. Tropp adds, "At Gallagher, every proposal that goes out has the Gallagher Way attached to it. This is how we share with people what we believe in."

Compliance and ethics

While many companies have programs wherein employees formally sign off on their review and understanding of legal compliance obligations, the ethical component is more difficult to document and make meaningful.

As Lisanne Sison, Managing Director, Enterprise Risk Management at Gallagher, adds, "It's absolutely crucial to be compliant, but merely meeting compliance standards is insufficient for managing an organization's reputation or helping it achieve its objectives. Therefore, without regulations, I think that an ethical culture is the driving force behind an organization."

"Doing business ethically, to me, means more than just focusing on profit," Sison continues. "It's about ensuring that your work aligns with your values and regulatory requirements and that you can trust the organization to do the right thing, even in the absence of specific, documented guidance. Ethical culture acts as guardrails to guide the organization when specific direction or policies are lacking."

"Compliance tells us what we must do, while ethics tells us what we should do," says Tropp. "Compliance is about adhering to the law and not violating any regulations. Ethics, on the other hand, is about beliefs, values, and culture. In our company, these two aspects often intersect."

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Minimizing the risk of damage through ethical behavior

Reputational factors, though less tangible than the numbers on the quarterly balance sheet, are nevertheless of vital importance in reducing long-term risks.

Ethical companies can be more attractive to clients and, importantly, to talented employees — fueling success, while unethical behavior can create risks such as reputational damage and costly legal actions.

Public perceptions of the degree to which a company behaves ethically (or unethically) can ultimately affect revenue generation. A company's ethical stance, then, becomes a central pillar of its financial success.

"When identifying an organization's biggest threats and determining the best ways to manage them," comments Sison, "the key to thriving comes down to organizational culture, which is driven by ethical behavior, values, trust in leadership, and the purpose and direction of the organization."

While there are examples of successful corporations enjoying continued success despite multiple instances of bad press or legal action, it's nevertheless advisable for all companies to consciously consider their own "ethical footprint" to ensure they are enabling their teams to make informed decisions with regard to how their behavior is perceived externally and how it aligns to their core values.

"Every company has a culture, whether good, bad, or indifferent," comments Ray Iardella, Vice President, Investor Relations at Gallagher. "If I were an investor, I would want to have conversations with management and understand the culture before investing."

Documentation and reinforcement at every level of operation are needed to minimize the risk of reputational damage. Tropp comments, "I believe it's crucial for companies to publicly demonstrate what they stand for. We've documented what ethical practices look like to us so that we can reinforce it across all our teams and behaviors. It's essential to make business values accessible to the world so that people can see what a company believes in."

And this need doesn't stop in the business world, in November 2023, the US Supreme Court adopted its first formal code of conduct governing the ethical behavior of its nine justices.

Does this mean the Court was not acting in an ethical manner before 2023? Of course not. However, codifying an organization's definitions of right and wrong behavior is an important tactic to align internally on values, ensure consistency in actions across the organization, and influence public perception.

This external brand image is critical to long-term reputational factors that feed sustainable success.

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Being ethical — and being recognized as such

It's worth noting that the growth of ethical behavior in business can only really be measured internally. Tropp observes, "Quantifying the values of a company is challenging and is something external organizations may struggle with."

Advertisers certainly have a keen understanding of this: According to a Statista August 2023 survey among chief marketing officers (CMOs) in Canada and the United States, 56 percent of respondents said they were allocating between 11 and 40 percent of their marketing budget to the promotion of business sustainability efforts.

Tropp comments, "I genuinely believe that a substantial portion of the reason we are seeing a heightened focus on these matters is because people are learning about them through social media platforms."

Iardella points out, "Demonstrating ethics is challenging as it cannot be easily benchmarked against financials. However, we strive to showcase it by encouraging interaction and transparency during earnings calls and investor days. We want to be open and transparent about our views, as it aligns with being both a good citizen and ethical."

Managing new risks resulting from deep-seated changes

Increasingly, the challenge is to embody a set of authentic values that permeate a company's whole culture.

With the increasing role of ethical practices in business success, coupled with individual employee perceptions of ethics, how can a company mitigate potential ideological conflicts when making critical business decisions?

Tropp comments, "In my opinion, if a company wants to showcase its values, it should start by examining its own operations." The key is for everyone in the company to understand the company's ethics and to embody them every day in their work.

The shift from hierarchical to circular business culture

Until the end of the 20th century, the top-down hierarchical "shareholder" model dominated how business was done. Here, the CEO's primary responsibility is profit maximization in order to grow value for the shareholders.

Towards the end of the 20th century, the "stakeholder" model gained traction. Here, the CEO's primary responsibility is to bring value to all stakeholders.

"Our mission statement includes four stakeholders: clients, employees, insurance carrier partners, and shareholders," notes Iardella. "We prioritize taking care of our employees, developing and growing them. Clients are crucial to our business, and insurance carrier partners provide the products we sell. If we fulfill our responsibilities to these stakeholders and conduct ourselves in the right way, shareholders are likely to be rewarded."

Rigid Structure of a Rule-Based Culture

Dictated from the top

↓

Executed from the middle

↓

Accepted by the stakeholders

Stakeholder vs shareholder decision-making

While the stakeholder model stresses a wider set of priorities than the shareholder paradigm, shareholders are nonetheless also interested in a company's ethical dimension. Iardella points out, "Some shareholders in our base focus on ethical behavior and prioritize companies they perceive as being at the forefront of ethics."

Here, as elsewhere, it's essential that a company's ethical position is perceived to be authentic, with a set of embedded practices carried out by engaged, empowered personnel rather than a notional, rhetorical commitment.

The circular culture and the engaged employee

The emergence of the stakeholder model was paralleled by a shift towards companies using their employees' insights to improve the way the business operated.

"This shift," says Tropp, "led to the development of a more 'circular' business culture — one where ideas and input from middle management and employees were valued and implemented. This concept of listening, requesting input, and respecting it became the foundation for developing a company's culture. Change and authenticity can only come from within, drawing on the commitment and expertise of all staff. It's the internal dynamics and culture of the company that truly drive change. This is how good cultures in corporations evolve and are maintained."

The senior management cohort plays an essential role in establishing and maintaining a "circular" culture: without senior managers' buy-in and demonstrable commitment to seeking and taking on board feedback, the circular flow of information and reality-led improvement will seize up, and the wheel of the virtuous circle will stop turning.

Beyond the implications of the stakeholder model and the idea of a circular culture, the question of how employees engage with their work is another factor in the ethical risk equation.

A recent LinkedIn survey showed a 154% increase in entry-level job ads featuring culture and values over the previous two years; job postings that mention values such as culture, flexibility, and well-being now receive nearly three times more views and twice as many applications.

Risk Placement Spectrum

Stakeholder — Value Oriented
- Lack of effectiveness
- Wandering by committee
- Mission shift
- Financial failure

Shareholder — Goal Oriented
- Loss of public respect
- End justifies means
- Human casualties
- Loss of support community

Digital risk exposure

The closer alignment of employees' personal values with their work, coupled with the parallel desire to influence what happens in the workplace via the circular model, could be seen as reflections of broader trends in society that have been facilitated by "digital democratization."

As well as opening an infinite supply of alternative viewpoints, where once upon a time gatekeepers limited the breadth of discussion, the internet has created avenues for individuals to share information about companies and their behaviors more quickly and widely than ever, creating another risk vector for companies.

Employees' desire to align their own values with the company's values can contribute to risk mitigation.

Iardella points out, "It can be challenging for organizations, especially larger ones, to consistently demonstrate ethical behavior. With the number of employees and their access to the web and social media, a company's reputation can be at risk from a small group of individuals. Therefore, it stands to reason that maintaining trust, ethical behavior, and transparency becomes more difficult as a company grows."

"However, if a company can uphold these values, it demonstrates how deeply ingrained the behavior is throughout the organization. While no large organization can get everything right, if instances that call into question ethical behavior are not happening frequently, it strengthens the argument that the behavior truly permeates the organization. It's certainly a more challenging task, but it also strengthens the case that your business or organization is different and can be sustained over time. So, it works both ways."

Embedding an ethical culture

"Walk the Talk"

Changing culture is hard, and often involves a change of leadership or a new vision. Commitment to change of this kind requires embodiment of values from top to bottom.

For example, Sison says, "Studies I've seen recently indicate that executive and senior leaders are more likely to declare that their company has a strong ethical culture than are individual contributors and front-line employees. This is a gap in alignment that can lead to risks for those organizations."

Iardella adds, "When companies are trying to present themselves in the best light, there can be a difference between how they present themselves externally and what is embedded in their culture.

In my experience, companies that are overly aggressive about trying to present themselves as super ethical or super focused on sustainability really aren't doing all the things that should be integral to their organizations."

"You really need a new vision and a long-term process to ensure that vision is spread throughout the organization. It keeps coming back to leadership; it starts at the top. An organization either has it or it doesn't, and it's challenging to make significant changes."

Iardella continues, "Observing leaders' behavior is crucial. If you see your boss handling an issue in a certain way, you might be inclined to follow the same path. It's contagious."

Conclusion

The risks related to reputation management and staying competitive are influenced by the changing landscapes of ethical behavior in business, shareholder and stakeholder interests, employee aspirations, and the internet's ability to broadcast vulnerabilities.

Statements of values, acting as a flag to rally around, are an important part of embedding a set of ethical practices and behaviors if the statements are authentic and are adhered to from leadership down. As Tropp emphasizes, "It's crucial for companies to demonstrate publicly what they stand for."

Likewise, the provision of a robust reporting system, coupled with a credible investigation and disciplinary process that is understood and trusted by employees, is also key.

Generational and societal shifts will keep coming: stasis is no longer an option. A company can benefit from documenting its ethical stance as a consistent decision-making framework. Monitoring how this — and, vitally, the way ethics are put into practice — affects a company's ability to respond to changing circumstances, and has a measurable impact on talent and its profitable and sustainable growth.

"Ethics are subjective, and so determining whether a business is following 'ethical practices' cannot be judged simply by evaluating against a checklist. Subjectivities must be presented as well," closes Tropp. "When it comes to our business, people don't buy from companies; they buy from people. They are introduced to a company through individuals and start doing business with the company. It all starts with the people."

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