

## WHY ARE CODES OF ETHICS IMPORTANT IN THE BUSINESS ENVIRONMENT?

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### ABSTRACT

*The aim of this paper is to explore the roles of ethics codes in the business environment. We will survey three types of ethics codes: those developed in business organizations, those developed at the professional level, and the voluntary industry codes. It is argued that at each of the three levels codes of ethics have three very important roles to play: moral guidance, providing support for those who are under pressure to act in an unethical manner and compliance with moral norms. While these three functions will be found at each of the three levels, we show that significant differences appear.*

**KEYWORDS:** *codes of ethics, compliance, guidance, support, voluntary industry codes.*

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### 1. INTRODUCTION

In this paper, we will examine the functions of the code of ethics in the business environment and the criteria that should be satisfied in order for them to fulfill their purpose. Codes of ethics started to appear in United States in the first half of the 20th Century and became used extensively in the 80s (Mureșan, 2009, 104). Today, codes of ethics have become very popular as an instrument to develop an ethical climate both in the public and the private sectors. Codes of ethics are usually developed in business organizations, at the professional level and at the industry level. Our article will be concerned with the functions of these three types of codes. We will focus on three very important functions: guiding behavior; supporting those who want to comply with ethical standards, but are under external pressure to act unethically; and ensuring compliance, through formal and informal mechanisms. We will begin our analysis by examining the roles of organizational codes of ethics and, in the second part of our paper, we will highlight the specific elements of the professional and industry codes of ethics, from the perspective of the same three functions mentioned above.

### 2. ORGANIZATIONAL CODES OF ETHICS

Organizational, or corporate, codes of ethics have three important roles: to guide the behavior of the employees, to protect those that have come under pressure not to act ethically and to sanction those who fail to comply with ethical norms. These are the three roles that we will examine in this section.

Firstly, codes of ethics provide guidelines for ethical conduct. Some authors criticize codes of ethics for being futile if the company does not enforce moral norms (Baker, 2007). It is true that there is no enforcement instrument of codes of ethics external to the company. Instruments of enforcing

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moral codes within organization become essential for their efficiency. Nevertheless, the guiding function of the codes should not be overlooked. In organizations and beyond, most people act fairly as long as they do not have a significant interest to do otherwise. Even more so, this should be true in organizations, as employee selection process should be based on criteria of integrity. Ethical values provide motivation; judging an action as morally desirable implies being motivated to act in that way. Therefore, moral values provide a drive for moral action. Still, the critic would continue, even without codes of ethics employees know how they should behave and, thus, codes of ethics do not bring anything new in this regard.

It is true that codes of ethics include values, principles and norms that are generally known and accepted at the level of the organization. This is undeniable, as the content of a code of ethics should express the values and principles that generate the consensus of the whole organization. Nevertheless, the fact that employees, in some cases helped by an outside consultant, systematically focus upon identifying the problems specific to the organization and upon the precise formulations of the provisions can help make the code of ethics an essential instrument in the ethical guidance of the members of the organization.

In order to be useful tools, codes of ethics must meet some conditions. First, codes of ethics should contain adequate norms and principles, which answer, as much as possible, to all relevant ethical issues in the organization. The provisions that are found in codes of ethics must not be formulated in a metaphorical or ambiguous language. It is very important that the persons who are responsible with developing a code of ethics identify completely and correctly the problems of the organization, so as to cover all possible moral difficulties that employees may face. Codes of ethics should not avoid problems that can generate difficult situations from a moral point of view. It is true that the concise provisions of such a code cannot be sufficient to solve ethical problems, but they can contribute to stating the general norms and to identifying the relevant elements involved in the ethical evaluation of a difficult situation. For example, suppose that an employee finds out his company has made an important deal with a supplier whose general manager is the employee's brother. For the time being, the employee's job description has nothing to do with her brother's firm, but it is very possible that, in the future, she will receive the task of testing the products that are supplied. If the company's code of ethics stipulates the fact that employees should always communicate any situations in which they are in a conflict of interest, be it actual, perceived or potential, then the employee in our example will be aware of ethical issues involved. However, general moral norms can come into conflict, and such situations are usually difficult to solve in a code of ethics, since many specific details of the cases might be relevant.

Secondly, codes of ethics should be systematically organized. Generally speaking, codes of ethics include four sections that need to be clearly distinguished. The introduction should contain a summary of the code's objectives and identification of the subjects (employees and, respectively, other stakeholders) that should respect the provisions. The second section should include the values and principles that must guide activities in the organization. Moral values are ideals that employees in the organization must aspire to. Integrity, the respect of other persons and justice represent such values. Ethical principles are general prescriptions that provide guidance regarding what actions are morally correct.<sup>1</sup> The third sections should include the ethical norms that the employees in the organization adhere to. Ethical norms are moral rules that are less general than principles and that forbid or prescribe certain actions. The fourth section includes sanctions. Moreover, the section dedicated to moral norms needs to be organized by separating the duties towards employees, consumers, environment, etc.

Thirdly, both at the principles and at the norms level, the provisions should have adequate degree of generality and proper ethical content. Ethical principles are a critical part of a code of ethics because they provide a foundation for the norms. Codes of ethics must focus upon values and principles that are relevant for the organization's field. Values and principles mentioned in codes of ethics are not necessarily specific to certain professions or areas of activity and can be relevant to

many professions and organizations. For example, confidentiality is a value that has a place in the codes of ethics developed for different organizations in a large range of fields. Codes of ethics must always express its principles in the form that is most relevant for the respective field.

Moral norms, even though their content is more concrete than that of principles, must not be overly detailed, going beyond the boundary of ethical concerns. Based on the codes of ethics, organizations can design documents that specify in detail norms for certain issues, like conflict of interest. It should also be highlighted that codes of ethics are different from codes of conduct. Though both contain standards regarding employee behavior, codes of ethics include norms that provide general guidance, which allow agents the freedom of action, while codes of conduct offer more determined rules regarding employee conduct in specific situations (Wood & Rimmer, 2003, 184). Although some norms in the codes of conduct have an ethical dimension, a code of conduct does not include ethical norms as such, but the specific rules employees must respect, in order to comply with the general professional or ethical standards.<sup>2</sup>

Fourthly, codes of ethics should include obligations to all stakeholders (Schwartz, 2002, 30), not just toward the company. Sometimes, codes of ethics are excessively focused on banning actions that harm the company, becoming, in this way, exclusively tool for the protecting the company. For example, there are codes of ethics that contain a general requirement that any off-the-job activity that can affect performance at the workplace is banned. This kind of provision is unacceptable, as it constitutes an excessive intervention in the employees' personal lives. A code of ethics should not overlook the norms that protect stakeholders such as employees and clients. For example, an important provision that should be found in a code of ethics of a bank is that the employees have to provide complete and correct information to clients, in order for them to make informed decisions. Moreover, employees must be protected from the illegal or unethical orders that may be given by management. It is recommended that a code of ethics must specify that this kind of orders should not be followed by employees.<sup>3</sup>

The second function of code of ethics is supporting employees in their commitment to act ethically. Codes of ethics – at least the good ones – provide support to the members of the organization who want to act ethically, but are pressured by the employers to break the moral rules. Returning to the previous example, if a company's code of ethics mentions that employees will not be punished if they do not comply with unethical orders, this provision functions as a mean of protection for employees who do not wish to comply with such orders.

The third function of ethics codes is that they improve the employees' compliance to norms. In most organizational codes, compliance is ensured through sanctions. Some authors consider that including sanctions in a code of ethics only serves to remove the moral dimensions of its provisions, and turning into a code of legal rules. The very nature of ethical norms involves the absence of sanctions in the case of not conforming to them (Ladd, 1991, 131). It is true that moral norms are not primarily described through external sanctions, such as written warnings or salary. Still, the mere fact that codes contain sanctions does not turn them into legal documents. As we have mentioned above, ethical provisions allow for more discretion than legal document do. In addition, codes of ethics have an important dimension involving guidance, which is missing from legal documents. We can accept, on the other hand, that most code of ethics – those that include sanctions – have a quasi-legal character, being placed between documents that have exclusively a compliance role and those who do not include any sanctions.

### **3. PROFESSIONAL CODES OF ETHICS AND VOLUNTARY INDUSTRY CODES**

Professional codes and those designed at the industry level have largely the same functions as those identified above. There are, though, certain differences that will be the examined in this section.

Professional codes are developed generally at the level of professional organization. They are much older than the organizational ones; the Hippocratic Oath, guiding medical practice since the 5th

Century BC, can be considered the first code of professional ethics. Many fields that are regulated through codes of ethics face many difficult ethical problems arising constantly in the professionals' activity. Criminal defense lawyers are often in the situation when they could discredit through unethical means the truthful witnesses. Physicians often consider that they should withhold truth from patients, in order to protect their health. That is why guidance in professional codes of ethics is even more important than in the case of organizational codes.

The most general principles of professional codes are proposed taking into account the purpose of the profession and the main objectives that must be achieved by professionals working in that field. For instance, the purpose of journalism is to disseminate information; the most general principles, without which the journalist cannot accomplish this purpose, have the central position in a code of ethics for journalists. Situations that lead to difficult ethical dilemmas are generated by conflicts between the principles that govern profession. This general approach leads to a high degree of consensus over the types of difficult situations that professional codes of ethics should deal with and over the general principles upon which the professional ethics are built. Despite the fact that this general agreement is not always extended to the situations when the moral norms come in conflict, professional ethics issues are debated by professionals as well as by ethics experts, which increases the probability that the provisions in the codes are useful as a guide in ethically difficult situations.

Regarding the role of supporting ethical conduct, professionals from various fields – for instance accountants, engineers, doctors, and lawyers – do not work on their own, but are members of business organizations, which have their own goals, not always coherent with the requirements of professional ethics, and this can lead to conflicts. Construction companies prefer sometimes speed over safety, media companies often avoid publishing compromising information on the companies that buy advertising space in their newspapers. In these situations, codes of ethics and professional organizations offer protection against the pressure coming from employers. Professionals working in organizations must comply both with the duties towards public and their employers; professional codes of ethics mention both types of obligations. Professionals are required to be loyal to their employers and to further their legitimate interests. On the other hand, in most cases when the employer's interest goes against the public interest, the latter should prevail.

Moreover, codes of ethics protect the personal values of professionals. For instance, in some countries, medical codes of ethics allow doctors to refuse for reasons of personal conscience to perform certain treatments and medical professionals can use this type of clause as an instrument to protect their values. Moreover, powerful professional organizations can impose ethical provisions in the national legislation. Finally, the protective role of professional codes of ethics has yet another dimension. Professionals are competing for clients and, thus, are under pressure to forgo ethical requirements. Codes of ethics punish this conduct, protecting professionals who act in an ethical manner from the unfair competition of their fellows.

The last aspect of professional codes of ethics we will discuss refers to sanctions. In some professions and countries, professional organizations control, by law, access to profession and can impose sanctions against those who do not comply with ethical or professional norms. In such professions, self-regulation has an important role for ethical compliance. In other cases, professional organizations do not have the same power to impose sanctions. The decision to join such an organization is voluntary, and the harshest sanction that this kind of organization can impose on professionals is removing them from the professional organization in case of ethical misconduct. In this situation, the compliance function of such codes of ethics is diminished.

The last kind of ethics codes we will examine are voluntary industry codes. They include the standards that companies in certain industries – together with other actors, such as NGOs – develop and choose to respect. The solution of self-regulation by the industry offers some benefits as compared to government regulation. Firstly, the companies in that field know the solutions to their specific problem better than the public authorities do. Voluntary codes avoid the dangers of over-

regulation and excessively costly solutions. Secondly, self-regulation can lead to faster ways of developing regulation, implementing measures and fixing problems (Castro, 2011, 5). Finally, if governments accept the solution of self-regulation, they don't have to spend precious resources for regulation and monitoring. Still, there remains a question whether self-imposed regulation will not be too soft, and this is the main danger of voluntary codes.

Like in the case of the other two types of codes, we can distinguish the three functions of industry codes: guidance, support and compliance. These codes guide the activity of companies that choose to adhere to them, through the standards regarding acceptable practices they stipulate. Such standards are generally more precisely and concisely formulated than provisions of organizational codes and tackle the critical problems of the industry, which regards the relationship between companies and stakeholders: employees, consumers, environment, governments, and society. Though the imposed standards are previously known throughout that industry, their formalization through codes at the level of the industry is meant to establish the norms as standard solutions, implicitly recognized by companies as feasible.

The industry codes of ethics have also the role of supporting companies that are willing to act ethically. Thus, when a company decides to comply with standards that its competitors fail to respect, this will incur high costs and bring a significant competitive disadvantage. This is why companies usually refuse to take unilaterally such a decision. Codes of ethics become a solution to this collective action problem. The "big players" in the industry agree to respect a set of norms, which "level the playing field", bringing the companies to the same level. Furthermore, like in the case of professional codes, the industry codes of ethics can in some cases serve as a mean of protection – in this case protecting the companies against governments' abusive actions. A good example for this is "Principles on Freedom of Expression and Privacy", a document advanced by the Global Network Initiative – an NGO that protects the freedom of expression and the privacy of Internet and mobile phone users and has as members the large companies of these industries. The document is meant as a "trump card" that companies can use when authoritarian governments want to impose regulations that damage freedom of expression and promote censorship.

The last part of this discussion involves the function of compliance. Given the fact that the adherence of companies to the industry codes is not mandated by law, the harshest sanction is the removal of the offending organization from the alliance that establishes and imposes the code. This sanction may seem symbolic, but in many industries the stakeholders pressure companies to comply with the standards agreed upon. For example, some investment funds can choose to invest only in companies that respect the standards established by industry codes. This kind of pressure brings gradual compliance. In order for this to happen, codes should establish a strong monitoring system, in which complaints are examined by neutral parts.

#### **4. CONCLUSION**

In this paper we discuss the roles of three types of ethics codes: developed in business organizations, at the professional level, and at the industry level. For each of them, we discussed three roles: guiding behavior, providing support for those under pressure to act unethically, and ensuring compliance with moral norms. Some significant differences appear. Professional and industry codes are focused on more specific ethical problems than organizational codes do. For this reason, their provisions are usually more precise and more useful as a guide to conduct. The second function, which of support, is more important for professional codes. Professional codes are often used by professionals as an instrument of protection against unethical requirements of the employers. Voluntary industry codes can be seen, more than the other two types of codes, as a solution to a collective action problem. The theoretical analysis in this article should be complemented by an empirical research on the efficiency of different types of ethics codes.

## ENDNOTES

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<sup>1</sup> For details and examples regarding ethical principles in a code of ethics, see Mureșan, 2009, 115-123.

<sup>2</sup> In practice, this distinction is fuzzy, and many companies develop only one code for both ethical norms and rules of conduct. Even in this type of code, the ethical norms are better to separate.

<sup>3</sup> For example, the Peterka & Partners (a Prague-based law firm) code of ethics stipulates: "No one in P&P is entitled to order you to carry out actions that would be illegal or unethical. P&P will never punish anybody for raising the question of legality and ethics. We all want to do the right thing." (<http://www.peterkapartners.com/en/code-of-ethics/>)

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