With the number of high profile corporate scandals by major companies such as WorldCom, Enron, and Tyco, as well as current firms such as India’s Satyam and the United States’ Countrywide Financial Corporation, Healthsouth Corporation, and Diebold Incorporated, inevitably the responsibility for such unethical conduct must revert back to the leaders of these corporations. It is no wonder that in a survey conducted by The Economist [October 2003] only 23 percent of those questioned believed that a corporate executive could be trusted, which was slightly higher than that of a used automobile salesperson. This article will examine: (1) Details of the lack of ethical leadership exhibited in the latter four companies mentioned above, (2) Several psychological and philosophical reasons why this behavior was able to transcend throughout the organization, (3) Some steps which should have been in place to deter this poor behavior by corporate leaders, and (4) Recommendations for future research.

Key words: corporate fraud, corporate leadership, corporate scandals, corporate social responsibility, unethical decision making

Lack of Ethical Leadership

In Sanskrit, satyam means truth. However, Satyam Computer’s founder and chairperson, Byyraju Ramalinga Raju, interpreted its meaning quite differently [Suchi, 2010, 47]. As India’s fourth largest computer exporter, stakeholders were shocked when Raju admitted to “cooking accounts” and falsifying revenue, which became even more egregious an action when PricewaterhouseCoopers’ auditors were accused of being accomplices by providing false numbers and verifying them for Raju [Suchi, 2010, 47]. In 2009, Raju admitted that he inflated key financial results for his firm by overstating profits for the past several years, overstating the company’s cash balance by one billion dollars, overstating the amount of debt owed to Satyam, and understating Satyam’s liabilities [“PCAOB,”
After a review, the Indian Central Bureau of Investigation believed the actual alleged amount of fraud was $3.02 billion ["Detecting Fraud," 2010, p. 12].

In this scandal, two auditors of Pricewaterhousecoopers were charged with accounting fraud, along with Satyam’s former chief financial officer, vice president of finance, senior finance manager, a managing director, and another director who were also indicted ["PwC India Auditors," 2009, p. 37]. Some critics have termed this “India’s Enron,” given several similarities in the modus operandi of the two firms, Enron and Satyam [Huber, 2009, January 15, p. 7]. At Satyam, two sub–accounts were controlled by Raju and some of his fellow executives—one sub–account was for the bank and the other was given to his unsuspecting accounting and finance teams [Koppikar, 2009, p. 31]. In addition, Raju allegedly created fake invoices—one given to his clients and the other inflated for his firm’s balance sheet. In another unethical action, he gave his accounting/finance teams one set of inflated cash receipts, while another set to the bank, which was a lower amount [Koppikar, p. 31]. Like Enron, loans as well as potential losses for the fiscal year were not shown on the books. In Satyam’s case, the reason the loans were omitted on the balance sheet was because this would have raised a red flag. After all, why would a company have so many liabilities, if it had such a large cash balance? [Koppikar, p. 31]. Unfortunately, the effect of this fraud extended beyond the investors and stockholders. When the fraud was announced, more than 14,000 employees put their curricula vitae on the Internet fearing the tenuousness of their careers at Satyam [Flinders, 2009]. Moreover, customers would be adversely affected if Satyam folded, since they depended upon the skilled services of Satyam’s accountants [Flinders, 2009]. Stakeholders in all arenas must pay the price of unscrupulous corporate leaders.

A second example of unscrupulous leadership occurred in 2010, when Countrywide Financial Corporation found its former chief executive officer (CEO), Angelo Mozilo, agreed to pay $67.5 million to the Securities and Exchange Commission in order to settle claims that he misled shareholders about the risks that were associated with the home mortgage loans assumed by his firm [Bronstad, 2010]. This was followed by David Sambol, former president of Countrywide and Eric Sieracki, former chief fiscal officer who were ordered to pay more than $5.6 million collectively for the same settlement charge as Mozilo [Bronstad, 2010]). The problem stemmed from the practice of approving home mortgages from many otherwise unqualified purchasers, without any regard to the risks that would be taken firstly by Countrywide and secondly by the stockholders or future investors.

In 2006, Michael Winston, an executive at Countrywide, who was hired to develop a solid growth strategy for the firm, noticed when he was first hired and entered the firm’s parking lot, a vanity license plate of an executive that read, “Fund’Em” [Morgenson, 2011]. This was a precursor for what was expected of all Countrywide executives.
For example, he once asked another executive, “what if an applicant has no job?” The response was, “fund’em” [Morgenson, 2011]. In another event, Winston found it odd that throughout his tenure at Countrywide, he was never shown the documentation for the exorbitant number of approved subprime loans (loans charging interest way below the prime rate) by his division. Later on, when questioning these liberal loan approval practices one too many times, Winston found himself without a job, which eventually led him to become a “whistleblower” against his former employer [Morgensen, 2011].

In another alleged 2009 breach of ethical leadership in this firm, a former Countrywide manager was brought up on charges by a Congressional House Committee, which accused him of giving Senate Banking Chairman Christopher Dodd and Senate Budget Chairman Kent Conrad “VIP” mortgage discounts from Countrywide. Dodd and Conrad were charged as well, but claimed that they were unaware of the special low mortgage rates, and vehemently have always denied such an accusation [“Loan Officer,” 2009]. If such an alleged conflict of interest existed, which by some counts it did, it is even more apparent how the corporate culture of this firm encouraged their executives to conduct business unethically [“Loan Officer,” 2009].

In another controversial situation, five former chief fiscal officers pleaded guilty and testified that Richard Scrushy, founder and CEO of their firm, HealthSouth Corporation, led them to a scheme to inflate earnings by $2.7 billion [“Ex–Health South,” 2005]. Ten other HealthSouth executives have also pleaded guilty since 2003 after testifying to prosecutors that since 1996 HealthSouth switched from “aggressive accounting” to outright fraud and not only inserted false numbers to cover up their earnings shortfalls, but even coined a name for itself, “the family” [“Ex–Health South,” 2005].

In 2004, Healthsouth agreed to pay the United States government $325 million for the allegations that it defrauded Medicare and other government health programs, even though Scrushy’s case by the government was dropped [“Healthsouth Settles,” 2006]. However, by all accounts, Scrushy earned hundreds of millions in bonuses and share sales, owned a personal yacht, a private jet, sponsored a female band called 3rd Faze, and hired a former television star to run the public relations firm during his tenure at Healthsouth in 2003 [Moynihan, 2003]. Yet, in 2005, the company promised to pay the Securities and Exchange Commission $100 million over five years to settle this accounting fraud charge, which resulted in losses to its stockholders as a consequence of this fraud [“Healthsouth Settles,” 2006].

In the final corporate example of unethical leadership, according to the Securities and Exchange Commission (SEC), the executives of Diebold Incorporated, manufacturers of automated teller machines, were found to have manipulated its earnings for several years to meet its financial performance forecasts. It did so by recording revenue before shipping its sold merchandise to buyers (called “bill and hold”), recognizing rev-
The revenue on lease agreements even though they were subject to “buy-back agreements” that nullified the revenue, and improperly delaying and capitalizing expenses that falsely increased the value of used inventory, all which breach generally accepted accounting principles (“SEC Charges Diebold,” 2010; Green, 2010; Kom, 2010). Eventually, the SEC filed charges against several former and current executives at Diebold, which included the former chief fiscal officer, controller, and director of accounting, who were all complicit in these actions that led to the charges previously cited (Green, 2010). In the words of one SEC director of enforcement, Robert Khuzami, “Diebold’s financial executives borrowed from many different chapters of the deceptive accounting playbook to fraudulently boost the company’s bottom line” (Green, 2010).

**Unethical Leadership: Psychological and Philosophical Reasons**

Perhaps one rationale for leaders to be tempted to walk down the unethical path in decision-making is that according to J. Singh of Wharton University of Pennsylvania, “we … judge a person simply by the amount of wealth he accumulated,” which he termed the *missing soul* [Singh, 2004, p. 59]. This section will examine some psychological reasons why executives conduct business unethically, as well as the philosophical reasons why such behavior is unacceptable. The psychological areas to be discussed are ego, overconfidence, self-esteem, stress, and workplace bullying. The philosophical motivator is many times utilitarian, which is implementing a decision when the majority of favorable outcomes exceed the negative ones.

According to Singh, one reason executives are willing to fabricate company performance is due to their inflated egos, which cause them to manipulate financial data so they are able to convince their stakeholders that all is well [Singh, p. 61]. Furthermore, based upon his research, Singh found that upper level executives today focus upon the “bottom line” and are less concerned with other stakeholders such as employees or society [Singh, p. 57]. As a result, these leaders become motivated by the rewards associated with their compensation, which many times are unrelated to their company profits, lucrative stock options, and other perquisites that further enhance the incentive to be deceitful.

In another study, this one, by Australian management professor Stephen Chen of Macquarie University in Sydney, it was found that a CEO’s overconfidence will cause him or her not to inflate earnings for self-benefit, as most research indicates, but rather to compensate for the misjudgment of the true performance of this leader [Chen, 2010, p. 37]. This causes the CEO, who may have initially formed an erroneous estimate of performance, to search for more evidence to support the initial estimate, even if it results in incorrect figures [Chen, p. 37]. Chen’s research also found, as other research has, that
psychological factors such as narcissism exist when the CEO may have an unusually high need to have his or her superiority reaffirmed, which is followed by applause, adulation, power, prestige, and glamour [Chen, p. 37].

In a 2010 study by Avey, Palanski, and Walumbwa, it was found that a negative correlation existed between ethical leadership and self-esteem [Avey, Palanski, and Walumbwa, 2011, p. 579]. In other words, those who had low self-esteem were more likely to follow ethical leadership than those who had high self-esteem. A corollary of this is that an executive with high self-esteem may ignore the ethical leadership of his or her company. The correlation between one’s self-esteem and one’s response to the ethicality of the company proves to be an interesting anomaly.

Stress is another factor that influences unethical decision-making. In a study by Selart and Johansen it was found that a significant positive correlation existed between stress and unethical behavior [Selart & Johansen, 2011, pp. 130–131]. When asked why they would consider being unethical, the majority of executives gave work overload, powerlessness, fear of punishment, or seeking approval as the motivating factors for their responses [Selart and Johansen, pp. 130–131]. When analyzing the Satyam fraud case, global risk consultant Steve Wilford, a national manager for an Indian firm called Control Risks, stated, “in times of stress, instances of companies stealing from each other and themselves tend to increase” [Anand, 2009, p. 19]. This supports the study by Selart and Johansen, which attributes stress to rationalize why executives are encouraged to be unethical.

In their review of literature, Bulutlar and Oz (2009) found that a positive correlation existed between workplace bullying and unethical behavior. Workplace bullying (or workplace rankism) is when a superior abuses hierarchical power at the expense of the subordinate [Lecker, 2010, p. 146]. In their review, Bulutlar and Oz found that bullying prevails when the organization approves of it, and is further encouraged when it reaps certain types of financial rewards [Bulutlar and Oz, 2009, pp. 275, 277]. So, if an employee is bullied into conducting business in an unethical manner by a bullying superior in order to increase profits, the bully will be rewarded for the positive financial outcome. Furthermore, the principle of utilitarianism is applied in this case, since the benefit of earning more profits outweighs the harm of the unethical behavior or the effect it may have on the victim who is bullied (Bulutlar and Oz, 2009, p. 276).

However, from a deontological viewpoint, which bases decision-making upon the intent of the action as opposed to the results expected from the action, unethical behavior is not acceptable in any terms, regardless of the outcomes it may produce. For brevity purposes, I will focus upon one philosopher, Immanuel Kant, best known for his deontological “golden rule” viewpoint, of “doing onto to others as you would want others to do onto you.”
According to Kant, one should, “Act in such a way that you always treat humanity, where in your own person or in the person of another, never simply as a means, but always at the same time as an end” [Kant, 1964, p. 96]. Kant believed that universal laws could be developed when there were no exceptions. Treating individuals unethically would never pass the test of an accepted universal law. After all, how would the corporate executive feel if he or she was the recipient of his or her own actions? At this point, given the psychological reasons why poor executive behavior occurs and a brief philosophical rationale for its unacceptability in the business world, we should examine what steps should be taken to ensure that the corporate executive is always at a high level of ethicality.

**Steps to Rectify Unethical Leadership**

The business world is faced with some unscrupulous leaders who affect the public’s view of all corporate leaders. There needs to be some accountability on the part of all members of the corporation to ensure that it follows the right moral compass when conducting business. This section includes recommended strategies that organizations must develop if they want to institutionalize ethical behavior as a core value.

In Singh’s article, “Rekindling the Heart and Soul of Management,” he depicts several recommendations for ensuring corporate accountability and ethicality among the firm’s executives (2004). Some of them are: appoint only those leaders who value and respect others, instead of the traditional “bottom line” of profits; invent new measures such as “Total Returns to Community;” include an evaluation of the means employed by which the profits and revenues are generated, not just the financial outcomes; and be a socially responsible company by first evaluating your community’s needs and then selecting a few areas where your contributions can make a “meaningful difference” [Singh, 2004, pp. 62, 63, 65].

Another set of recommendations to improve the ethicality of a firm is to: allow managers to make mistakes so they are not pressured to conceal their errors; develop a code of ethics that must be disseminated and discussed by all employees; conduct unscheduled audits of your own business practices; discuss ethical issues in performance appraisals; establish a reward system for exemplary ethical conduct; publicize any unethical behavior after confronting it swiftly with harsh penalties; and hold joint question and answer meetings with your attorneys, accountants, and investment bankers in conjunction with your upper level executives, middle managers, and front line supervisors in order to have an open system of checks and balances in place [Gandossy and Kanter, 2002, pp. 419–421].
A preventative measure that has been implemented and studied in research by Castiglia and Nunez found that all the coursework offered in an M.B.A. program, which integrated ethical decision–making and was embraced by the entire college community, would benefit its graduates who represented most of the future executives of our major firms [2009, p. 42]. In their study, it was found that 40 percent of the top–ranked business schools in the United States required only one stand–alone corporate ethics course for their students. However, after taking the course, although initially it would raise the moral compass of their ethical values, in time these students would revert back to the same ethical codes that they had practiced prior to taking the course [Castiglia and Nunez, p. 42]. As Aristotle espoused in his virtue ethics, “virtue of character results from habit” [Irwin and Fine, 1995, p. 366]. Perhaps, requiring M.B.A. programs to integrate ethics in all their courses is a step in that direction.

Another recommendation is to address one of the first recommendations: How do you identify potential leaders who will be ethical? Several measurements such as the Defining Issues Test and more recently the Managerial Moral Judgment Test have been developed using scenarios that then identify the level of ethicality for each given individual based upon his or her response to the scenarios presented in the test [Loviscky, Trevino, and Jacobs, 2007, pp. 263–264]. Although not a precise predictor, it does accomplish two goals: First, it attempts to separate how ethical a potential employee may be, and secondly, it espouses a message to the applicant that being ethical is a prerequisite for success at this company, where he or she is applying.

Other recommendations for instilling more ethical decision–making may be to (1) create an ethics officer position, so if there is a question by another employee on whether a particular action is ethical or a potential whistleblower does not want to be forced to take his concerns outside the organization, this individual will be a resource person, plus it will allow employees a sense of confidentiality, (2) develop an Ethics Committee that, like an ethics officer, serves the same purpose, but does so in a collective capacity, and (3) institute a decision–making model that includes ethics as a criterion, instead of just looking at its effects on profit, and includes examining the effects of a particular decision on its stakeholders [Lecker, 2010, pp. 116–121]. For an organization to be ethical, various programs and approaches need to be institutionalized for this to be accomplished.

Future Research

In order to prevent corporate leaders from behaving badly, further research is required. Even though some psychological reasons were addressed in this article, what are other psychological reasons that executives do not follow a just moral compass? Why are some ethical leaders able to prevail over a corporate environment that does not support ethical
decision–making? What are some decision–making models that are used by successful business, which are profitable and ethical? How does an ethics officer compare to an ethics committee in reducing unethical behavior? What are the traits of ethical leaders who are able to influence subordinates on the cusp of ethicality? These are just some research areas that should be examined in the future.

Conclusion

In a survey by The Economist, it was found that since the CEOs set the ethical tone in their businesses, they play a large part in helping to regain public trust that has been lost. Chinese philosopher, Guanzi once said, “If a person rises to a level of authority that exceeds his virtue, all will suffer” [Singh, 2004, p. 59]. Perhaps, the Western, as well as the Eastern world should take note of this philosopher, as one cure for executives who behave badly is to hire only those with the ethical wisdom to conduct business justly.

References


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