

# 20 Questions

Directors Should Ask about  
Codes of Conduct

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The Canadian Institute  
of Chartered Accountants

## How to use this publication

Each “20 Questions” publication is designed to be a concise, easy-to-read introduction to an issue of importance to directors. The question format reflects the oversight role of directors, which includes asking management — and themselves — tough questions.

The questions are not intended to be a precise checklist, but rather a way to provide insight and stimulate discussion on important topics. In some cases, Boards will not want to ask the questions directly but they may wish to ask management to prepare briefings that address the points raised by the questions.

The comments that accompany the questions provide directors with a basis for critically assessing the answers they get and digging deeper if necessary. The comments summarize current thinking on the issues and the practices of leading organizations. They may not be the best answer for every organization.

Thus, although the questions apply to any organization, the answers will vary according to the size, complexity and sophistication of each individual organization.

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# Preface

The Risk Management and Governance Board of the Canadian Institute of Chartered Accountants (CICA) has developed this briefing to help members of Boards fulfill their responsibility for the oversight of an organization's ethical climate. It is intended primarily to help individual directors but boards may also wish to use it for orientation and discussion.

The oversight role of a director includes assuring themselves that the organization's culture is characterized by ethical practices and business behaviour. This briefing provides suggested questions for boards to ask the CEO, senior management, professional advisors — and itself. We hope that directors and CEOs will find it useful in assessing their present approach to formulating or revising Codes of Conduct and to ensuring that the principles of these Codes are practiced throughout the organization.

We also hope that reading this document will prompt dialogue among directors and between boards and executives. That's exactly what an effective Code should do, and what we are seeking here.

The Board thanks the authors — Michael Gunns and Mark Wexler — and acknowledges the contribution of the Directors Advisory Group, who advises the CICA. They identified the need for research and guidance in this important area and have provided high level coaching suggestions to the authors throughout the course of their work.

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Chair, Risk Management and Governance Board

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# Why directors should ask questions about Codes of Conduct

Today, an increasing number of organizations have a Code of Conduct — far more than even a few years ago. Until recently, however, many boards have been only peripherally involved in reviewing Codes and ensuring that they are effectively implemented and executed.

In parallel with boards' increasing involvement in strategy and risk management, directors are recognizing that Codes of Conduct are key factors in influencing an organization's reputation and success. Like strategy and risk management, the responsibilities associated with developing and implementing an effective Code are shared between the board and management — management usually designing materials and processes and the board approving them and ensuring that they are effectively implemented.

Accordingly, this document has been prepared in two principal sections:

- A. Code context, development and revision; and
- B. Code implementation and execution.

Where an organization has an existing Code, and where directors are generally confident in its relevance and content, boards may choose to focus primarily on the questions in section B — implementation and execution. Where a Code is being introduced for the first time, or where a major revision or relaunch of an existing Code is planned, directors may also wish to become more familiar with the questions in section A — context and development.

Many smaller organizations will not need to introduce the formality of structure or process described in several places in this document. The principles, however, remain the same and we are confident that directors will use their intimate knowledge of the individual organizations they serve in tailoring their enquiries and assessing responses. Several of the highlighted sidebar comments in this document reflect this less formal perspective.

A Code is always a work in progress — it's better to make a start with an unsophisticated Code, developed or revised according to sound principles, than to lose the benefits of having one — or, worse, to promote a Code that's irrelevant or unrealistic.

**//** But we must remember that good laws, if they are not obeyed, do not constitute good government. Hence there are two parts of good government; one is the actual obedience of citizens to the laws, the other part is the goodness of the laws which they obey... **//**

*Aristotle*

## Section A — Code context, development & revision

### 1. What are the objectives of the Code of Conduct?

A Code of Conduct (“Code”), championed by those in leadership positions in an organization is a key vehicle for:

- setting the boundaries of acceptable behaviour;
- reducing the risk and associated costs of fraud, conflicts of interest and other ethical lapses;
- helping introduce new employees to the organization’s standards;
- attracting and retaining high calibre employees and business partners;
- providing employees and others subject to the Code with comfort that they will not inadvertently stray offside;
- informing contractors, suppliers and others doing business with the organization of its expectations regarding acceptable behaviour;
- providing the basis for sanctions against those that deviate from the Code.

Providing a framework of shared boundaries allows people to vigorously pursue goals and objectives while confident that they, and those they rely on, won’t stray offside.

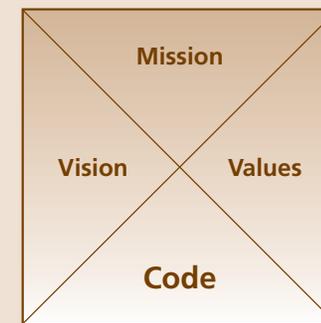
Organizations, which walk the talk with regard to their Code, develop a reputation for honesty, integrity and principled business behaviour. Effective Codes also reinforce an organization’s culture by emphasizing each individual’s responsibility to observe its principles and requirements. Ultimately, it is this culture of shared responsibility that affords the greatest protection against the risks of unethical behaviour.

On the other hand, merely issuing a Code does not assure an organization that it will be observed. Organizations that issue Codes simply to fulfill legal requirements or in response to stakeholder concerns, yet do little or nothing to embed the principles, invariably sow the seeds of cynicism.

### 2. What is the Code’s relationship to the organization’s mission, vision and values?

Codes are rarely stand-alone documents. In most organizations, Codes are introduced or revised within an existing context of explicit directional and behavioural expectations.

Whereas statements of mission, vision and values may be expected to inspire employees and other stakeholders in achieving organizational objectives, a Code has a different purpose. A Code sets boundaries of acceptable behavior. Positioned correctly, an appropriate Code completes the picture of an organization’s aspirations and expectations.



### 3. Is the Code at the right level for the organization?

Codes that establish unrealistically high levels of behaviour expose the organization to vulnerability. On the other hand, a Code that merely repeats or summarizes existing legal requirements is likely to be seen as a token effort.

Establishing a Code of Conduct in an organization offers significant potential benefits. It also exposes the organization to risks.

Where exercising individual discretion is inherent in conducting the organization's business it will also be necessary to decide the extent to which this should be considered and reflected in its Code.

Finally, the time frame over which the Code is expected to influence the organization's culture should be considered. Successfully introducing and embedding a Code within an organization is, itself, an important change initiative. Most successful change initiatives take time and many are best approached as a continuing process, rather than a quick fix. On occasion, however, there is a need to make major changes in behaviour quickly to avoid exposure to legal or reputational risks.

The chart set out in Appendix 1 summarizes each of these factors and potential benefits and risks associated with choosing different alternatives.

### 4. How does the Code relate to the organization's culture?

An organization's ethical climate is significantly influenced by its leadership. A term often used for this influence is "tone at the top". It creates the overall context in which all of the organization's directional statements (including the Code) are interpreted. Some factors that can influence the ethical climate of an organization include:

- the nature and influence of its shareholders;
- the regulatory environment (which may require specific standards);
- the country or countries in which it operates;
- its "ethical history" — good or bad;
- its short and long-term rewards structures;
- the behaviour of its contemporaries and competitors;
- the perceived consequences of ethical breakdowns in terms of financial and reputational loss.

An organization's ethical climate also influences many key dynamics surrounding a Code and its effectiveness. If people feel free to raise issues, the likelihood of problems being hidden until they develop into major crises is significantly reduced. The right to dissent usually and properly varies according to the circumstances and the nature of the organization's business.

**///** Why? Let me try to explain...Firstly, we often don't see the need to observe our laws because these laws are broken all around us before our eyes — and quite often!... Can it really be the Government Commission that accepted Block 4 as ready for operation did not know that it was accepting it as incomplete? Of course they knew... **///**

*Excerpt from transcript — Chernobyl Disaster*

Codes combine three interrelated areas of content that relate to the organization's culture, as follows:

- aspirational content;
- descriptive content; and
- proscriptive content.

Most organizations will be best served by a Code that is largely descriptive in nature and includes only the proscriptive content that is essential to its particular circumstances.

The **aspirational** content of a Code is idealistic and can be related most clearly to the organization's mission, vision, values and long-term goals.

The **descriptive** content of a Code outlines the specific behaviour sought by the organization in areas such as conflicts of interest, the acceptability of gifts from customers and suppliers, and other similar areas where the organization seeks to establish its particular position. The descriptive content is largely silent with regard to sanctions for specific Code violations.

The **proscriptive** content of a Code sets out what the organization prohibits. This "thou shall not" material increases the clarity of the Code. However, if this content is dominant within a Code, it may impede proper risk-taking and limit innovation. The proscriptive content also lends itself to forbidding behaviours that, although legally permissible, are unacceptable to the organization.

The overriding objective is to create a Code that appropriately balances aspirational, descriptive and proscriptive content. Each organization must find the appropriate balance between these three components.

## 5. Has the organization determined its actual ethical risks?

Although many of the topics that will typically be covered in a Code are common across organizations, the practical exposure to ethical risk may vary considerably. Exposure to specific ethical risks may also vary widely across the different parts of an individual organization. Before the introduction of a Code and at regular intervals thereafter, an organization should make an assessment of its exposure to specific ethical risks. The results of this assessment will bring valuable perspective to the emphasis to be placed on individual parts of the Code.

A key input to the assessment will be the organization's awareness of previous breakdowns in ethical behaviour and the resulting losses, if any. Wider industry history, or the experience of others with similar exposures, may also prove to be invaluable in assessing risks.

As organizations increasingly adopt formal risk management processes, it is important to integrate the results of an ethics audit into the overall risk assessment process. Sometimes, it might seem that ethical lapses would typically have less impact than, say, overlooked strategic risks. However, one only has to look, for example, at the implosions of Enron and Arthur Andersen to appreciate the very real consequences and costs of poor ethical behaviour.

“We can afford to lose money, even a lot of money. We cannot afford to lose our reputation, not even a shred of it.”

Warren Buffett

## 6. How does the Code apply to foreign operations?

Operations in countries other than an organization's home base can present many complications, not the least being how to apply its Code in other jurisdictions and cultures. An organization that is serious in its pursuit of foreign operations should measure the ethical risks as part of its strategy towards those operations — both before entering the environment and regularly thereafter. These risks include not only exposures to loss or censure abroad but also the impact in the organization's home country of real or perceived ethical shortcomings in overseas operations.

Simply following a policy of “When in Rome, do as the Romans do” is unlikely to serve an organization well when it comes to ethics. Many organizations have paid dearly in terms of damaged reputations as a result of media attention to local child labour practices, weak environmental controls, and the like, in overseas operations. The intellectual arguments that: “it's necessary to meet the local competition” or “it's expected locally”, may be technically correct but are unlikely to convince today's public.

“Plausible deniability” is also unlikely to save a CEO or a board of directors if weaknesses or poor practices are highlighted, particularly if an organization is blamed for observing lower standards away from home.

Realistically,  
“Don't ask, don't tell”  
has become:  
“You'd better ask, and you'd better tell”.

## 7. Who are the champions of the Code?

### The role of the board of directors

The board of directors, itself, should be subject to the Code and its obligations go further. It has a key leadership and governance role in ensuring that the Code is not only appropriate to the organization but that it is consistently applied. This commitment is reinforced when directors individually sign off on the Code (see Question 14).

Directors often underestimate the significant individual and collective influence they can and should have over signaling to the CEO and the rest of the organization what is expected and acceptable behaviour.

A diligent board should carefully study any new Code or revision, before approving it, to ensure that it is suitable and capable of being implemented. The board can also act as an invaluable resource and guide to the CEO. The varied perspectives and experiences of individual board members can generate wise counsel to the CEO as to the suitability of the Code to his or her organization and the potential risks in introducing or monitoring compliance with it.

Finally, the board is also responsible for ensuring that its own actions and those of the CEO (whether or not a member of the board) are consistent with the Code. As such, they become the first and most important part of setting the tone at the top of the organization, from which all other behaviour follows.

### The role of the CEO and executive team

Establishing, disseminating and supporting a Code are leadership activities. Accordingly, all stakeholders will focus on the CEO's personal association with the development of the Code and how it is implemented and executed. Typically, the CEO will appoint others (e.g., a chief ethics officer) to create and maintain the Code and to monitor its application. The organizational relationship of this individual or individuals to the CEO, their personal credibility and the support and resources they are afforded will all be used by stakeholders as indicators of the CEO's personal commitment to the Code. Accordingly, one way or another, the CEO must be the ultimate champion of the Code, if it is to be taken seriously.

**//** If ethics are poor at the top, that behaviour is copied down through the organization. **//**  
*Robert Noyce — "Mayor" of Silicon Valley*

The senior executive team also has a key responsibility in ensuring that the Code is embraced and followed by the rest of the organization. This team represents the first potential for a break point within the organization between espoused practices (the Code) and actual behaviour. An apparent lack of interest or, worse, cynicism on the part of the CEO's direct reports will immediately send a message to the rest of the organization that the Code is not to be taken seriously.

### 8. Who develops, administers and maintains the Code?

Although the CEO and the board of directors champion the Code, its development, periodic revision, administration and maintenance is usually delegated to an individual who may also head up a function dedicated to the Code and related ethical matters.

In all organizations, the CEO is the ultimate "chief ethics officer".  
In small organizations, he or she may be the only "Ethics Officer".

In large organizations, the individual assigned these responsibilities may be termed a "chief ethics officer" or the role may be assigned to an existing chief compliance officer. In somewhat smaller organizations, the responsibility may be assumed by the head of, for example, the Law Department, or by the Corporate Secretary. Small organizations may engage an external consultant on an as needed basis to draft and revise Codes. External advisors can also contribute valuable advice and perspective to organizations seeking to ensure that their Code represents best practice.

As noted in Question 7, it is extremely important that those assigned to developing, revising and administering the Code be viewed as credible and impartial.

## 9. What is the process for developing the Code?

### Stakeholder participation

Although the initiative for a new or revised Code usually emanates from the top of the organization, the timing and manner of inclusion of the representative views of other constituencies is a key factor in the Code being widely adopted and followed.

/// There can be no true agreement without the opportunity for discussion and negotiation. ///

*Giles Meikle — Corporate Director*

There are two principal constituencies that should be involved in the Code's creation. The suggested manner of reflecting their views is as follows:

#### Fiduciary stakeholders

Those having a direct fiduciary relationship with the organization would typically include the board of directors, employees, major suppliers and contractors. Best practice is to establish representative teams from each group subject to the Code and to engage them in a participatory process. In the case of directors and employees, the organization will seek input on both content and wording. In the case of suppliers and contractors, it is more a matter of discussing alignment of business practices and behaviours.

Smaller organizations, in particular, will find that they can get stakeholder input without resorting to a bureaucratic approach.

The most important thing is to demonstrate respect and... listen.

#### Other stakeholders

Other stakeholder groups will legitimately have an interest in the content and application of the Code. Depending on the organization's particular circumstances, this might include environmentalists, union representatives, regulators, or special interest groups. Although seeking input from these groups is not obligatory, including them in the development process can afford the opportunity of building stronger relationships and trust with them.

#### Expert input

It is essential that those developing or revising the Code consult frequently with the organization's legal expert, whether an internal lawyer or outside counsel. Other technical specialists in areas covered by the Code (e.g., investment traders, environmental specialists, etc.) should also be consulted.

#### Supplementary Codes

One important way of guarding against unnecessarily long and detailed Codes is to recognize that some material is only relevant to a particular part, or parts, of an organization. Examples would include detailed insider trading requirements for investment personnel, supplier relationships for purchasing departments, etc. In these and similar cases, it is appropriate to have supplementary Codes for particular activities and functions.

Certain professionals engaged in the organization may also be subject to the Codes of Conduct of their own professional bodies. An organization's Code supplements, rather than overrides or limits the application of these professional Codes in a similar manner to which it supplements relevant laws and regulations to which the organization is subject.

## Simple language

Each organization, industry, and region tends to have its own particular style of communicating.

**//** If a code consists merely of broad, vague concepts, the code may also not be sufficiently clear and specific to allow employees to understand what conduct is expected of them. **//**

*Mark Schwartz — A Code of Ethics for Corporate Codes of Ethics*

The probability of satisfying varied readerships can be increased by:

- structuring the Code in a manner where general principles or policies are stated as briefly as possible, followed by more explanatory text;
- the use of practical examples — either as part of the text or as “sidebars”;
- the use of pictures and graphics to emphasize key points;
- making reference to appendices or additional sources in technical areas (e.g., detailed insider trading policies).

Where organizations operate in different countries, it is vital to make sure that not only are the translations of the Code into different languages accurate but that they convey the intent and not just the actual written word. Different cultures place differing weights and interpretations on moral and ethical principles. It is essential to ensure that the Code’s readership receives and understands the intended message.

If in doubt, leaders should ensure that the words and tone used are similar to those they would use in a one-on-one discussion with a front line employee.

## 10. What is the process for the periodic review and revision of the Code?

A Code is always a work in progress. Key factors influencing the need to revise a Code include:

- changes in the organization’s business, or the environment or locations in which it operates;
- changes in relevant laws and regulations;
- public opinion regarding acceptable business behaviour
- experience gained from monitoring infractions, or difficulties in applying the Code;
- input received from those subject to the Code (including the organization’s leadership) regarding missing elements, unclear language or other weaknesses in the Code.

The most important factor, however, demanding regular review of the Code is to evidence the continuing commitment of the organization’s leadership to it.

Even with today’s rapidly changing business environment, twelve months will rarely have sufficient impact on a well-crafted Code to justify an annual formal revision and reissue.

If appropriate effort is put into developing the Code, in the first place, its fundamentals will change little over time. However, language, examples and specifics will change as the business and regulatory environment changes.

A more practical approach is as follows:

- a commitment to review the contents and applicability of the Code at least annually;
- an annual report to the CEO and the board (see Question 18) that the Code remains generally appropriate, and describing areas where revisions are contemplated;
- a full revision, reissue and formal re-endorsement of the Code by the organization's leadership every three to five years. This is also a suitable time frame for an organization-wide re-education in the Code, even if the content is not significantly changed.

The method for this comprehensive review, revision and reissue of the Code would correspond to that used for developing the Code (Question 9). Interim changes or supplements to the Code or other explanatory material would follow a similar but less comprehensive process, particularly since they often affect only one part of an organization or a relatively narrow aspect of its activities (e.g., new privacy regulations).



## Section B — Code implementation and execution

### 11. How is the Code communicated and how are people educated in it?

#### Communication

In today's media-rich world, organizations have the opportunity to disseminate information in many different ways. Key factors in choosing communication channels include:

- accessibility;
- user receptiveness;
- interactivity;
- appropriateness to the subject matter.

Recognizing their importance and relative permanence, Codes will normally be distributed in printed form, at least to the principal stakeholders such as the board and employees. However, there are many opportunities to supplement the written document with other forms of distribution.

Some examples of organizations that make their Codes available on the Web are:

- Brascan
- Coca-Cola
- GE
- Petro-Canada
- Royal Bank
- Verizon.

Making the Code available on an organization's website allows ready access by existing and potential investors, customers, suppliers and other stakeholders. It also provides immediate topical access to those

who may already possess a printed copy but do not have ready access to it. Web access can also provide faster and easier access where supplemental materials are referenced in the Code but would be too extensive to conveniently include in a printed version.

#### Education

Individuals have many demands on their time and, legitimately, cannot be expected to study in detail every communication they receive. Additionally, Codes of any substance will address behavioural matters that are subject to different interpretations.

Leading organizations use many approaches, and often a combination of them, to educate employees (and others subject to the Code) in its principles and requirements. These include:

- presentations by the organization's leaders and their availability for questions and dialogue;
- discussions between supervisors and their employees;
- videos and web-based educational materials;
- briefings for suppliers and contractors.

**//** A recent survey conducted by the Canadian Centre for Ethics and Corporate Policy found that corporations that create a code of ethics are often flummoxed when it comes to turning it into more than just pieces of paper stashed away on a dusty shelf. **//**

*Laura Bogomolny — "Good housekeeping: How to ensure your code of ethics is effective," Canadian Business, March, 2004*

Although some of these communication vehicles will be necessarily one way, interactive sessions are what really bring a Code to life. Participating in discussions gives those subject to the Code the opportunity to raise and discuss its practical application. It also (if an appropriate system is established) provides invaluable input to those responsible for Code revisions. Business circumstances change so rapidly that what seemed straightforward when a Code was issued can quickly become irrelevant or unsuitable.

Some organizations use ethical dilemmas, case studies or quizzes to spark debate amongst employee groups. These can be very useful when a Code is first introduced or to refresh interest in the Code. For example, some organizations use online ethical quizzes as a precursor to annual electronic Code sign offs.

While delivering documents to an executive, Sue overhears that a division will likely be closed. Sue's daughter works for that division and is about to take out a large mortgage on a new house.

Will Sue tell her daughter what she's heard? Should she?

However, overusing poignant dilemmas can become counter-productive. An organization's ethical climate is established more by the day-to-day actions of its leaders and the ongoing conversations between its employees, than by occasional shock therapy.

Education also has an important role with regard to new employees or other business partners. Many organizations provide orientation sessions for new hires and this is an appropriate vehicle for initial education in the organization's Code. Leading organizations, however, will cover this orientation before an offer is extended to a prospective employee, supplier or contractor. This provides far greater assurance that both the organization and those it engages are willingly committed to its Code from the outset.

Accordingly, organizations will find that using a variety of methods that influence its everyday workings towards maintaining an ethical perspective in all of its actions will ultimately best deliver their goals.

## 12. How does the organization handle criticism of the Code?

Regardless of the amount of effort devoted to designing and developing it, any Code will have its critics. Some will see the Code as unnecessary (believing appropriate behaviour is self-evident), others may feel the Code goes too far or fails to be completely precise.

Some criticism is to be expected. How the organization handles it, however, demonstrates its true commitment to its principles and beliefs.

Statements in Codes of ethics are most likely to have an impact when they address new situations or when they take positions with which one mildly disagrees.

*Bruce Gamatz and John Lere —  
Certified Planning Journal, 2003*

Acknowledging and listening carefully and respectfully to critical input to the Code is of paramount importance. Undertaking to consider these opinions and views in subsequent revisions of the Code is also appropriate. Bending to the expectations of vigorous critics, at the expense of the organization's well thought out and purposefully developed principles, however, will quickly weaken everyone's commitment to the Code and can lead to widespread cynicism.

It is essential that the organization establish an explicit process for handling criticism of the Code. Typically this will include the individuals and functional areas mentioned in Question 8.

### **13. How is compliance with the Code measured and monitored?**

The fact that people are aware that compliance with the Code is being monitored acts as encouragement to follow its intent. It also strengthens the Code by reassuring everyone that the protection it affords is actively maintained.

A further reason for monitoring compliance is to develop an ongoing understanding of where breakdowns in expected behaviour may be occurring, in order to discern patterns of weakness — either in organizational culture or Code design. This information serves as input to the established revision process or, where breakdowns are consequential, to timely supplements to the Code or the introduction of measures to mitigate risks associated with non-adherence to the Code. Where monitoring reveals significant or pervasive weaknesses, this information should also influence the organization's overall risk management process.

The most usual methods of measuring and monitoring compliance include:

- annual surveys;
- focus groups or interviews;
- informal conversations;
- one-on-one discussion during annual performance reviews (supervisors can elicit common themes or issues);
- feedback from those administering “hot lines” for employees to report actual or suspected Code transgressions;
- exit interviews;
- internal audits;
- external reviews.

As mentioned in Question 11, some organizations use an online ethics quiz as a precursor to asking for annual Code sign offs. Appropriately analyzing the trends of responses to these quizzes can also offer considerable insight into the degree to which the Code is understood and respected.

In measuring and monitoring compliance, there is an important distinction to be drawn between investigating infractions and seeking assurance that the systems and processes surrounding the Code are effective.

Indirect measures of ethical performance, such as surveys and focus groups, can be more important than “hard” measures.

Sometimes, hard measures can have unintended results — e.g., measuring the actual number of reported Code violations can actually discourage people from reporting them.

Both of these types of review have their place. Almost all organizations realize the need to investigate infractions. Fewer organizations dedicate themselves to systemic learning from these investigations (rather than merely dealing with transgressors and plugging gaps). The best organizations adopt and follow a formal and comprehensive program of ongoing systemic review embodying some, or all, of the methods mentioned above.

#### 14. Do we ask people to sign off?

Organizations typically ask those subject to its provisions to confirm in writing that they:

- received a copy of the Code;
- understand its contents;
- commit to applying it.

Additionally, many organizations ask directors and employees (and others subject to the Code) to complete such a sign off annually — reconfirming their continuing commitment and explicitly stating that they have followed the requirements of the Code throughout the previous year. Sign off forms should make provision for disclosure of incidences of known or suspected non-compliance on the part of those completing them. New employees should be asked to complete a sign off as a condition of employment.

Recent legislation in the United States requires formal confirmation by the directors, and those within the organization who are responsible for the accuracy of financial systems and disclosures, to confirm that their Code contains suitable provisions in this regard, and that they have been adhered to. Canadian regulatory authorities are contemplating similar requirements.

Since the great majority of organizations will have at least some proscriptive content to their Code, they should seek sign offs (typically annually). Some organizations choose to request sign offs only from officers or those otherwise subject to the proscriptive elements of the Code (e.g., investment dealers, accounting personnel, purchasing staff, etc.). However, in many organizations such designated individuals can constitute a large proportion of its employees. In such cases, it may be appropriate to have everyone sign off on the Code to avoid creating an aura, in some, of a lack of importance either of their position or their commitment to the organization or the Code.

If in doubt, implement an annual sign off for everyone.

In most organizations, the majority of employees have access to the organization's computer systems and customer information — both of which need to be carefully safeguarded.

Legal requirements or the detailed proscriptive elements of a Code may require more detailed and specific sign offs from those in senior positions or holding specific roles. Such detailed sign offs should be tailored to the circumstances, as should sign offs from contractors, suppliers or other parties subject to the Code.

Asking people to regularly sign off on a Code can, and should, keep the Code front of mind. It may also cause individuals to come forward with real or perceived difficulties arising from past or anticipated actions or circumstances. It is vital that these cases are handled respectfully and in accordance with an established and transparent process. Typically, this process will be similar to that described under Question 15.

Paper-based sign offs continue to be the most usual, although some larger organizations have introduced web-based electronic sign offs. In these cases, the usual precautions prevail regarding assuring the authenticity of the electronic signature and its relationship to the undertaking made.

### **15. Where do people go for advice, issue resolution, or to seek a waiver of the Code's application?**

Despite using best efforts to develop a clear Code, circumstances will invariably arise where either the exact circumstances were not contemplated by the Code, or where the application of the Code is unclear.

A Code of Conduct is not "law" — at its best it represents a common agreement on behaviour between people working together.

If someone has a problem with the Code, it's better to hear about it and try to resolve it, than to ignore or suppress it.

Within the organization, an individual would normally first raise such issues with their immediate supervisor. Where this does not lead to satisfactory resolution, the supervisor may suggest taking the issue higher up the reporting line or he or she may, themselves, do so on the employee's behalf.

Circumstances may arise where employees are reluctant to discuss a matter with their supervisor, either for fear of retribution or because they suspect wrongdoing on the part of the supervisor. The Code should offer explicit guidance to be followed in these circumstances. Typically the channels for such enquiries will include the chief ethics

officer, the chief compliance officer or the head of the Law, Human Resources or Internal Audit functions.

External stakeholders such as customers, suppliers and investors should also have an explicit point within the organization to contact with questions regarding the organization's Code. These questions should be directed to the chief ethics or compliance officer, if the organization has appointed one. Otherwise, questions might be directed to the Public Relations department or the Corporate Secretary who, if necessary, will forward the question to the appropriate party for a response.

There may be occasions where employees or others subject to the Code will seek to have its provisions waived. To discourage people from seeking relief from what they perceive as inequitable treatment from the strict application of the Code ultimately acts as an incentive to cover up.

Although such requests should be rare, there should be an explicit process for people to seek such waivers. This will typically require deliberation at senior executive levels and, usually, at the board level. All waivers granted, regardless of significance, should be reported to the board of directors.

### **16. How does the Code relate to the rewards system and how are violations handled?**

Perhaps the most difficult aspect of making a Code work is how to link it to rewards and sanctions. Some organizations specifically claim that sound ethical behaviour is a component of their rewards structure but, understandably, there is little publicly available evidence in this regard.

In most organizations, however, there are opportunities to identify instances where difficult choices were made that respected the intent of the Code. Although there may not be many opportunities to publicly recognize these occurrences, if everyone in the organization is attuned to the Code's purpose it's surprising how the recognition of one person of the behaviour of another — “That must have been a difficult choice, I wonder if I could have been as principled” — can have significant impact. Even simply discussing difficult ethical decisions with one's supervisor or co-workers acknowledges the worth of their views and perspectives.

/// On an aircraft carrier, if a small wrench is lost, the ship closes down until it's found. A misplaced item on the flight deck could be sucked into an aircraft turbine — with fatal results. If it turns out that the mechanic miscounted his or her tools, they're still congratulated. ///

*Excerpted from Managing the Unexpected  
Karl E. Weick/Kathleen M. Sutcliffe*

The question of sanctions is more straightforward. That is not to say that the necessary actions will be easy or comfortable to take. However, an organization committed to its Code has no choice but to vigorously and relentlessly pursue any instance of transgression. This includes perceived transgressions, unless they are clearly ungrounded. To do otherwise is the fastest and most certain course to undermining all the efforts put into developing and implementing the Code. Worse still, it is almost guaranteed to quickly evoke cynicism and distrust.

Often, the exact circumstances surrounding the need for and nature of disciplinary measures cannot be made public. It is essential, however, that the organization is seen as having followed a fair and established process in examining all sides of a matter before imposing sanctions.

### 17. How does the Code deal with whistle blowing?

Effective Codes accomplish two goals with regards to whistle blowing.

Firstly, they help to create an organizational culture in which whistleblowers find it easier to raise actual or perceived wrongdoing within the organization, rather than turning to the media or other outsiders.

Wise organizations go out of their way to provide several internal avenues for raising concerns. They also provide an external whistle blowing hotline and encourage employees to use it when all other avenues have failed.

Secondly, effective Codes provide explicit protection to the whistleblower from retaliation by those adversely impacted by the whistleblower's actions.

In most instances, whistleblowers go to outsiders because they feel that:

- their views have not been, or will not be, taken seriously;
- their concerns relate to someone to whom they report, or who has other significant influence over them;
- the actual or perceived wrongdoing is harmful to others or to the public.

Effective Codes provide people who choose to blow the whistle with several options to speak candidly and confidentially about their concerns. Although the normal first course of action is for someone to approach their immediate supervisor, sound Codes explicitly provide other avenues for people to raise issues.

Providing multiple channels improves the likelihood that individuals will first seek to resolve issues and concerns internally. The avenues offered will depend on the circumstances and structure of the particular organization. If the organization has appointed a chief ethics or compliance officer, this person would be the most likely to demonstrate the personal credibility, objectivity and training to listen to concerns and provide counsel and support. In the absence of an individual clearly holding this position in an organization, the heads of the Law, Internal Audit or Human Resources functions are typically mentioned as being avenues through which to raise concerns. In some organizations, a specific investigations committee is established to consider issues and concerns.

The fairness and respect with which an organization treats whistleblowers is an acid test of its commitment to openness and transparency.

Increasingly, organizations are making use of specialist external “hotline” providers who operate under strict confidentiality and ethical guidelines.

One of the most difficult situations that an organization has to face is how to deal with anonymous complaints concerning ethical behaviour. Whether apparently from employees or other sources, they cannot be ignored. Each instance must be weighed on its own merits,

usually by those concerned with administering and maintaining the Code (Question 8).

### **18. What information should the board receive?**

The preceding questions outline how an organization and its board of directors can assure itself that its Code is:

- relevant;
- properly developed, championed, administered and maintained;
- supported by suitable education;
- accompanied by appropriate processes to assure compliance;
- accompanied by adequate channels for employees and others to express grievances or concerns.

The board of directors has a key role and leadership responsibilities in most of these activities. Exactly how the board discharges its role and oversight duties will vary from organization to organization. However, the chart in Appendix 2 summarizes the types of information and reporting that a board might typically expect regarding the organization’s Code of Conduct and supporting processes.

### **19. But, as a director, how do I really know the Code is actually working?**

Despite all best efforts in reviewing written documents and asking intelligent questions, many directors continue to have niggling doubts as to whether the principles of the Code are actually being practiced throughout the organization.

This is understandable. For some time, CEO's and other executives have been operating in an intensely profit-oriented environment. Through inadvertence or poor design, organizational reward systems have not always emphasized or encouraged ethical behaviour on the part of leaders or those they have supervised.

This does not mean, however, that poor ethical behaviour is endemic at all levels in a particular organization, or is widespread in organizations — just as bad leadership does not generally affect the overall morality of a nation.

**//** You're on ethical thin ice when you hear these warning signs...

- Well, maybe just this once
- No one will ever know
- It doesn't matter how it gets done, as long as it gets done
- It sounds too good to be true
- Everyone does it
- What's in it for me?
- We didn't have this conversation. **//**

*Mark Wexler — Confronting Moral Worlds*

It does mean that boards have an opportunity to re-affirm the importance of ethical behaviour and to use their best skills and experience to assess whether the organization's Code is actually being applied. In addition to the practices and processes outlined in the preceding questions, there are two other things that directors can do.

Directors can accept the responsibility individually, and as a board, to use their instincts and experience in assessing the actual behaviour of the CEO and other members of the senior management team — and to be prepared to discuss it openly amongst themselves and, if necessary, directly with the CEO. If this feels too uncomfortable, either within the board or towards the CEO, it's probably an indication that something's wrong.

Directors can use every opportunity to observe what is actually happening in the organization and to listen to what others say about it. Increasingly, directors visit plants and other parts of the organization. Simply asking a front line employee — “why is this a good organization to work for?” — will not only inform (and probably reassure) the director, it will also reinforce the importance of values and ethics in that employee and all the others he or she tells of the encounter. And, if a director feels uncomfortable asking, or feels there's no opportunity, it's probably a cause for concern.

Many directors find that “field” visits, when they chat informally with management and front line employees, are invaluable — not only to understanding the business but to assessing the organization's ethical climate.

They factor this assessment into their confidence in everything from the organization's survivability to the probable accuracy of its results and reporting.

At their root, Codes are concerned with behaviour — both organizational and individual. Directors are typically very experienced at assessing the correctness of their own instincts and observations. Doing so, and discussing concerns openly, is a key part of their contribution to the tone at the top.

## 20. How does an organization's Code stand the test of time?

Over time, organizations — all organizations — are tested. They are tested by whistle blowing incidents, product recalls, indiscretions by leaders, accidents that injure innocent third parties, and the like. Codes do not prevent these events from occurring.

Codes are a means of creating resilience in organizational systems. They are always a work in progress. It is only through ongoing dialogue among all the organization's stakeholders that the shared commitment of superior organizational behaviour is maintained.

By building and maintaining a culture of openness and mutual respect, an organization can protect itself from being blindsided — being the last to know.

**//** Ethics is an area where "practice makes perspective." **//**

*John Dalla Costa*

*From: The Ethical Imperative —  
Why Moral Leadership is Good Business*

The board of directors possesses one of the greatest funds of knowledge, experience and wisdom available to the organization it serves. Through its own contribution and by the example it sets to the CEO and the rest of the organization, it can encourage a culture of openness, healthy introspection and the pursuit of organizational excellence.



## Appendix 1: Potential benefits and risks associated with three key criteria of Code design (see Question 3)

Factor	Description	Potential Benefits	Potential Risks
How <b>high</b> should the standards of the Code be in relation to those established by existing law?	Organizations are required to follow the law. A Code only adds value if it establishes organizational standards where the law is silent, or sets standards above those legally required.	<b>Higher Standards</b> <ul style="list-style-type: none"> <li>• Maximum potential for superior reputation</li> <li>• Can build high esprit de corps</li> </ul>	<b>Higher Standards</b> <ul style="list-style-type: none"> <li>• Easy to be offside from the outset</li> <li>• Unrealistically high standards could reduce competitiveness and profitability</li> </ul>
		<b>Lower Standards</b> <ul style="list-style-type: none"> <li>• Less likely that the organization will start out, or become, offside</li> </ul>	<b>Lower Standards</b> <ul style="list-style-type: none"> <li>• May be seen as trite</li> </ul>
To what extent will the Code deal with areas requiring <b>individual discretion</b> and those where performance cannot be easily measured?	Some organizational activities are closely supervised and easily monitored. In other areas, expected behaviour is not self-evident and is capable of a wide range of reasonable interpretation.	<b>More Focus on Individual Discretion</b> <ul style="list-style-type: none"> <li>• Can support peak performance through appropriate empowerment</li> <li>• Can encourage organizational learning through discussion and assessment of alternatives</li> <li>• Can reinforce personal and organizational accountability</li> </ul>	<b>More Focus on Individual Discretion</b> <ul style="list-style-type: none"> <li>• Might encourage unnecessary ambiguity to the detriment of effectiveness and efficiency</li> </ul>
		<b>Less Focus on Individual Discretion</b> <ul style="list-style-type: none"> <li>• May be cheaper to develop</li> <li>• May be easier to monitor and enforce</li> </ul>	<b>Less Focus on Individual Discretion</b> <ul style="list-style-type: none"> <li>• May be seen as unnecessary — more as operational policy than a Code</li> </ul>
What is the <b>time frame</b> for enhancing the organization's culture?	A Code is an opportunity to enhance an organization's culture and to build a superior reputation over time. This requires making it a win-win proposition with those subject to it — rather than a quick fix.	<b>Longer Time Horizon</b> <ul style="list-style-type: none"> <li>• Recognizes that cultural change and building shared commitments are long-term processes</li> <li>• Usually a better fit with the time horizons of companion Mission, Vision and Values</li> </ul>	<b>Longer Time Horizon</b> <ul style="list-style-type: none"> <li>• Increases organizational vulnerability if there are significant gaps between Code expectations and present performance</li> <li>• Can encourage indefinite postponement of tackling tough issues</li> </ul>
		<b>Shorter Time Horizon</b> <ul style="list-style-type: none"> <li>• If supported by other significant change efforts, can quickly revitalize an organization</li> <li>• May be necessary if there are significant gaps between actual and required performance</li> </ul>	<b>Shorter Time Horizon</b> <ul style="list-style-type: none"> <li>• Unrealistic expectations can undermine people's commitment to the Code, leading to widespread cynicism and the possibility of real organizational vulnerability</li> </ul>

## Appendix 2: Typical formal reporting to the board on Code activities (see Question 18)

Topic	Frequency	Question Reference
A Drafts of proposed new or reissued Codes, including how they were developed and plans for distribution and training	as occurring	9, 10
B Briefing on responsibilities for maintaining and administering the Code, including individual and functional responsibilities	annual	8
C Results of any audits and their relationship to the organization's overall risk management activities	as occurring	5
D Annual Code review: <ul style="list-style-type: none"> <li>• Continued applicability</li> <li>• Date of contemplated next Code revision</li> <li>• Any addenda or supplements issued</li> </ul>	annual	10
E Results of ongoing compliance and monitoring activities	annual	13
F Results of systemic audits or similar reviews	as occurring	13
G Report on annual sign offs and the handling of exceptions	annual	14
H Report on Code waivers granted, or being considered	as occurring	15
I Report on Code violations and related sanctions	as occurring	16

## Appendix 3: Topics that may be included in Codes of Conduct

The following topics (listed in alphabetical order) are typical of those found in Codes of Conduct. This is not intended to be an exhaustive list but may be helpful when reviewing the content of a Code. Except in the largest organizations, Codes will rarely cover such an extensive number of topics.

1. Bribery of government officials or others
2. Charitable contributions
3. Computer security
4. Confidentiality
5. Conflicts of interest
6. Confirming compliance with the Code
7. Consequences of contravening the Code
8. Customer complaint handling
9. Discrimination
10. Drug use
11. Employment of spouses or other family members
12. Environmental policies
13. External directorships
14. Fair employment practices
15. Gifts and entertainment from suppliers and others
16. Gifts and entertainment to customers and others
17. Insider trading
18. Intellectual property and other propriety information
19. Maintaining accurate records
20. Media relations
21. Outside employment
22. Personal use of computer systems
23. Political activity
24. Privacy of employee, customer and other records
25. Product safety
26. Purchasing policies
27. Reporting violations and suspected violations
28. Responding to shareholder activists or other organizational critics
29. Regulatory enquiries
30. Safeguarding assets
31. Seeking a waiver from the Code's provisions
32. Supplementary Codes
33. Truth in advertising
34. Use of organization's assets
35. Whistle blowing procedures
36. Workplace harassment
37. Workplace safety

## Where to find more information

### Canadian Institute of Chartered Accountants publications

#### The 20 Questions series

*20 Questions Directors Should Ask about Building a Board*

*20 Questions Directors Should Ask about Codes of Conduct*

*20 Questions Directors Should Ask about Director Compensation*

*20 Questions Directors Should Ask about Executive Compensation*

*20 Questions Directors Should Ask about IT*

*20 Questions Directors Should Ask about Information Technology Outsourcing*

*20 Questions Directors Should Ask about Internal Audit*

*20 Questions Directors Should Ask about Management's Discussion and Analysis*

*20 Questions Directors Should Ask about Privacy*

*20 Questions Directors Should Ask about Risk*

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#### Other CICA publications on governance, strategy and risk

*Crisis Management for Directors*

*Guidance for Directors: Dealing with Risk in the Boardroom*

*Guidance for Directors: Governance Processes for Control*

*Integrity in the Spotlight: Opportunities for Audit Committees*

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# 20 Questions

Directors Should Ask about  
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