

Business Ethics

The Law of Rules



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BUSINESS ETHICS: THE LAW OF RULES*

Abstract

Despite the recent rash of corporate scandals and the resulting rush to address the problem by adding more laws and regulations, seemingly little attention has been paid to how the nature (not the substance) of rules may or may not affect ethical decision-making. Drawing on work in the law, ethics, management, psychology, and other social sciences, this article explores how several characteristics of rules may interfere with the process of reaching and implementing ethical decisions. Such a relationship would have practical implications for regulatory policy and managers of organizations, and the article concludes by suggesting how regulations and corporate ethics programs should be able to improve the ethical culture of business and enhance the ethical decision-making skills of employees.

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“One might suppose that where law is largely absent, behavior is pretty bad. Yet it turns out to be nearly the other way around. The two areas where law is arguably the *largest* presence in ordinary life – driving cars and paying taxes – are probably the two areas where there is the largest amount of self-conscious cheating.”¹

“NASA’s culture of bureaucratic accountability emphasized chain of command, procedure, following the rules, and going by the book. While rules and procedures were essential for coordination, they had an unintended but negative effect. Allegiance to hierarchy and procedure had replaced deference to NASA engineers’ technical expertise.”²

INTRODUCTION

Lower Manhattan, March 2, 2004: Martha Stewart, WorldCom’s Scott Sullivan, Tyco’s Dennis Kozlowski and Mark Swartz and Adelphia’s John Rigas were being prosecuted, all within two blocks of one another, when Attorney General John Ashcroft appeared at Foley Square to announce the indictment of Bernard Ebbers, Chief Executive of WorldCom.³ While perhaps lacking the same dramatic simultaneity and proximity, many other officials have been indicted by state and federal authorities, and still more have been named in civil enforcement actions, arising from the corporate scandals of the past several years.

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¹ William J. Stuntz, *Christian Legal Theory*, 116 HARV. L. REV. 1701, 1747 (2003) (reviewing CHRISTIAN PERSPECTIVES ON LEGAL THOUGHT (Michael W. McConnell et al. eds.) (2001)).

² 1 NAT’L AERONAUTICS & SPACE ADMIN., REPORT OF THE COLUMBIA ACCIDENT INVESTIGATION BOARD 200 (2003), available at http://anon.nasa-global.speedera.net/anon.nasa-global/CAIB/CAIB_lowres_full.pdf.

³ See Robert Frank, *The Gang’s All Here: ‘90s Highfliers Bring Day of Chaos to Courts*, WALL ST. J., Mar. 3, 2004, at A1.

These facts make it difficult to argue that law enforcement lacked an arsenal of statutes and regulations with which to charge companies and individuals for corporate misconduct.⁴ Moreover, the many guilty pleas and settlements suggest that defendants and respondents either were aware of applicable regulations and the difference between right and wrong, and that they were doing the wrong thing, or that they had concluded (on the basis of their own assessment or that of their lawyers) that the likelihood of persuading a jury or other fact-finder to the contrary was slight.

This should not be a surprise. Wall Street scandals arose in one of the most intensely regulated industries. Other corporate scandals – Enron and WorldCom to name only the most widely known – involved issues of finance and accounting, which are largely rule-based disciplines. This misconduct did not occur in a corporate "wild West" where lawlessness required that one make it up as one went along.⁵

Despite the many existing rules, prosecutions, and settlements, the response to the corporate scandals has been primarily rule-based.⁶ Congress passed the Sarbanes-Oxley Act of 2002.⁷ The Securities and Exchange Commission and other agencies have promulgated numerous regulations implementing Sarbanes-Oxley and addressing other corporate governance issues. The New York Stock Exchange and the National Association of Securities Dealers have adopted new listing standards and other governance rules.⁸ Business continues to develop new procedures, appoint governance officers, and train employees on their legal and regulatory obligations.

These regulatory developments arguably have been accompanied by a greater focus on ethics. Ethics consulting has increased in the wake of Sarbanes-Oxley;⁹ membership in the Ethics and Compliance

⁴ Donald C. Langevoort, *The Regulators and the Financial Scandals*, in RESTORING TRUST IN AMERICAN BUSINESS 63, 68 (Jay W. Lorsch et al. eds., 2005) (hereinafter "Lorsch") ("[W]hat many people have said in the aftermath of the scandals is true: everything that was seriously wrong violated existing rules or principles, so that the problem was not that the disclosure regime was filled with large holes.").

⁵ Rules must still be applied to particular situations, of course, which entails judgment and discretion. As discussed in this article, however, rules affect how these decisions are made and implemented.

⁶ "Rule," when used in this article, refers to statutes, regulations, and other prescriptions promulgated by governing bodies applicable to everyone subject to their authority. Excluded are "rules of nature," "rules of thumb," and *ad hoc* directives to fewer than all similarly-situated individuals.

⁷ Sarbanes Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified in scattered sections of the United States Code, principally Title 15) (hereinafter "Sarbanes-Oxley").

⁸ See NAT'L ASS'N OF SECURITIES DEALERS, MANUAL Rule 4350 (2003); NEW YORK STOCK EXCHANGE, LISTED COMPANY MANUAL § 303A (2003).

⁹ See Kris Maher, *Sarbanes-Oxley Is Boon for Slew of Consultants*, WALL ST. J., Aug. 19, 2003, at B1.

Officer Association has increased steadily and remains at an all-time high;¹⁰ and the recently-amended Federal Sentencing Guidelines now refer explicitly to ethics.¹¹ A closer examination, however, reveals that even these ethics developments have been largely rule-based. First, while some consultants focus on values, much of ethics consulting tends still to entail implementing statutory requirements or developing training programs on the legal obligations of employees. Second, the “ethics officer” and “compliance officer” titles are often interchangeable, and the role involves supporting regulatory compliance by the business and its employees. A report by the court-appointed corporate monitor of WorldCom, Inc. (viewed by many as a blue-print for governance generally), for example, describes the ideal ethics officer as someone with legal, regulatory, and law enforcement experience, who would report to the company’s General Counsel.¹² Yet, such a structure, whether the Ethics (or Compliance) Officer is a lawyer or a non-lawyer supervised by a lawyer, tends to influence the approach taken to ethics.¹³ Third, despite references to promoting ethical conduct, the Sentencing Guidelines actually define a “compliance and ethics program” as one “designed to prevent and detect criminal conduct”¹⁴ and would seem narrowly satisfied by a program limited to criminal activity rather than also to ethical or even civil law issues.

This post-scandal preoccupation with rules could have been predicted. In deciding how to behave in a situation, our inquiry often starts – and stops – with rules. Rules have become proxies for the “right” thing when the distinction between obeying the rule and acting ethically becomes blurred, when we hear “If

¹⁰ Telephone Interview with Edward S. Petry, Executive Director, Ethics and Compliance Officer Ass’n (Sept. 6, 2004).

¹¹ See U.S. SENTENCING GUIDELINES MANUAL § 8B2.1(a)(2) (2005), available at <http://www.ussc.gov/2005guid/gl2005.pdf>. In *U.S. v. Booker*, 543 U.S. 220 (2005), the Supreme Court invalidated a statute that permitted judges to depart from sentencing ranges on the basis of facts not pled to or found by a jury. Whereas the Court’s concern was with *aggravating* circumstances (*id.* at 244), a “compliance and ethics program” is a *mitigating* factor. Moreover, the Guidelines, while no longer mandatory, do have an advisory function (*id.* at 246). A “compliance and ethics program,” therefore, remains relevant for both judges and business managers.

¹² See RICHARD C. BREEDEN, RESTORING TRUST: REPORT TO THE HON. JED S. RAKOFF ON CORPORATE GOVERNANCE FOR THE FUTURE OF MCI 110 (2003), available at http://www.nysd.uscourts.gov/rulings/02cv4963_082603.pdf.

¹³ See Linda Klebe Treviño et al., *Managing Ethics and Legal Compliance: What Works and What Hurts*, 41 CAL. MGMT. REV. 131, 146 (1999). See also Scott J. Reynolds & Norman E. Bowie, *A Kantian Perspective on the Characteristics of Ethics Programs*, 14 BUS. ETHICS Q. 275, 286 (2004) (hereinafter “Reynolds & Bowie”).

¹⁴ See U.S. SENTENCING GUIDELINES MANUAL § 8B2.1(a)(2) cmt n.1 (2005), available at <http://www.ussc.gov/2005guid/gl2005.pdf>. The point here is not that the Sentencing Guidelines should extend to legal-but-unethical conduct, but simply that regulatory references to ethics remain largely limited to legal rather than ethical considerations.

it's legal, it's ethical,"¹⁵ or "As long as it's not illegal, it's okay."¹⁶ Rules have also triumphed over ethics when they become the ceiling rather than the floor for desired conduct – as when companies opt not to go beyond the minimum requirements of the code-of-ethics provisions of Sarbanes-Oxley, or when research analysts participated in sales calls in Europe when then-recent regulatory changes technically applied only to such meetings in the United States.¹⁷

Rules have significant limitations, however.¹⁸ Many of these limitations are well-known and have been widely considered. Some involve *scope* – rules are reactions to yesterday's disaster and cannot be developed to address crises that we cannot anticipate.¹⁹ Others involve *content* – rules can require acts that are morally reprehensible, such as those on which racial or religious discrimination is based. And still other limitations involve *language* and *currency* – the number, age, complexity, and clarity of rules affect whether rules will (or will not) succeed in controlling behavior.²⁰

But what if the *inherent nature* of rules also makes it more difficult to decide and do the right thing? What if the tendency to focus on the letter of the rule rather than its spirit, or to interpret rules technically and narrowly, or to push the envelope is due, at least in part, to characteristics of the rules themselves? The pages that follow consider just such a possibility, namely that rules might actually (albeit ironically and unintentionally) undermine ethical decision-making.

The debate over whether conduct is more effectively regulated by principles (standards) or rules, while not unrelated to this issue, need not be addressed here. First, although rules and principles *are* distinct, the distinction is not between law and morality: moral dictates can be as detailed as legal rules (*e.g.*, "children should give their seats to elderly people who board a bus"), and legal/regulatory requirements can be as broad as ethical principles (*e.g.*, due process; "fairly present in all material

¹⁵ See Lynn Sharp Paine, *Managing for Organizational Integrity*, HARV. BUS. R., Mar.-Apr. 1994, at 106, 109 (hereinafter "Paine") ("If it's legal, it's ethical,' is a frequently heard slogan. But conduct that is lawful may be highly problematic from an ethical point of view."). See also William H. Widen, *Enron at the Margin*, 58 BUS. LAW. 961, 999 (2003).

¹⁶ See Blake E. Ashforth & Vikas Anand, *The Normalization of Corruption in Organizations*, 25 RESEARCH IN ORG. BEHAVIOR 1, 18 (2003) (citation omitted).

¹⁷ See Erik Portanger, *Banned on Wall Street, But All Right Abroad?*, WALL ST. J., June 6, 2003, at C1.

¹⁸ See, *e.g.*, Rakesh Khurana et al., *Management as a Profession*, in Lorsch, *supra* note 4, at 43, 44.

¹⁹ EUGENE BARDACH & ROBERT A. KAGAN, GOING BY THE BOOK: THE PROBLEM OF REGULATORY UNREASONABLENESS 100 (2d ed. 2002) (hereinafter "BARDACH & KAGAN").

²⁰ See Diane Vaughan, *Toward Understanding Unlawful Organizational Behavior*, 80 MICH. L. REV. 1377, 1398-99 (1982).

respects”).²¹ The limitations of rules that are discussed below apply to both moral and legal rules. Second, the way that rules or principles are applied (whether their content is legal or ethical in nature) tends to cause them to converge:

When authorised to act in accordance with rules, rule-subjects will tend to convert rules into standards by employing a battery of rule-avoiding devices that serve to soften the hard edges of rules. . . . Conversely the adaptive behaviour of rule-subjects when given a standard goes in the opposite direction. These rule-subjects, when given few rules in the rules-standards sense, will make them themselves, and apply them to their own allegedly discretionary behaviour, thus limiting significantly the case-sensitive discretion that it was the intention of the rule-maker to grant.²²

If rules and principles are two ends of a continuum,²³ then precisely where on the continuum a particular prescription is located may not be crucial; it will eventually tend toward the middle.²⁴

To be clear: the point here is not that the ethical lapses involved in corporate scandals stemmed directly and primarily from rules. Surely other factors (including compensation structure, management’s preoccupation with short-term results rather than long-term sustainability, conflicts between business lines, greed, and a feeling of being “above the law”) played a role. Nor is the point that rules should be abolished; they will – and should – continue to be essential guides for conduct. Indeed, one should not overlook the ways that rules make certain freedoms possible and influence morality positively; statutes prohibiting racial discrimination, for example, required people to interact and, over time, some racial attitudes changed.²⁵

Yet, to ignore the effect of rules on decision-making would be a mistake for both regulatory policy and business strategy. First, many of the other causes of business misconduct are being addressed by new laws and rules; if rules are part of the problem, though, a remedy that relies unduly on rules will have limited success (and may even make the problem worse). Second, to minimize unintended consequences, rule-makers should be aware of the potential effect of their rules. Third, with an understanding of the

²¹ For a discussion of differences between moral and legal rules, see Steven Shavell, *Law versus Morality as Regulators of Conduct*, 4 AM. L. & ECO. REV. 227, 229-32 (2002) (hereinafter “Shavell”).

²² Frederick Schauer, *The Convergence of Rules and Standards*, 2003 N.Z. L. REV. 303, 312.

²³ *See id.* at 309.

²⁴ The extremes of the continuum have also been identified as “hypernorms” and moral rules, with moral principles – that are justified by the former and that generate the latter – lying in between. *See* Edward Soule, *Managerial Moral Strategies – In Search of a Few Good Principles*, 27 ACAD. MGMT. REV. 114, 120 (2002). Thus, even apart from any convergence, different definitions of “principle” in the literature (and different views of the relationship between principles and narrower and broader concepts) create challenges for comparing principles and rules. Because this analysis is not essential to the issue under examination, such a comparison will not be pursued here.

²⁵ *See* Shavell, *supra* note 21, at 254-55.

limitations of rules and the other factors that influence ethical action, rule-makers could require business to take steps – and business could undertake those steps even without such rules – to strengthen ethical decision-making by employees.

The paper proceeds as follows: The first section considers certain characteristics of rules, particularly their inherent incompleteness and dependency on sanctions. The second section describes ethical decision-making, and how rules may actually interfere with that process. A greater focus on ethical decision-making may be *desirable* even without a showing that rules impede that process; it would be *essential* if such a showing could be made. The third section, therefore, suggests steps that regulatory and business communities might take to encourage ethical conduct and stronger ethical decision-making skills by employees.

SOME CHARACTERISTICS OF RULES²⁶

Rules control our tendency to act only in our self-interest. Even where we are not entirely selfish, however, rules remain important. People have different perceptions of themselves, one another, and the situations they confront, and different views of what is ethical (or otherwise appropriate) in such circumstances. Without rules of the road, some well-meaning drivers would drive slowly, others would drive quickly, believing (correctly) that they were doing so safely, and still others would drive quickly but not as safely as they thought they were – with a collision the all-but-certain result.

Section 406 of Sarbanes-Oxley, requiring public companies to disclose whether they have adopted a code of ethics, illustrates the reason for and utility of rules. The provision requires not just *any* code of ethics: companies must disclose whether they have a code that covers the “principal financial officer and comptroller or principal accounting officer, or persons performing similar functions.”²⁷ Moreover, having *some* code to which those officers are subject is not good enough; the code must address the following specific issues:

- (1) honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships;
- (2) full, fair, accurate, timely, and understandable disclosure in the periodic reports required to be filed by the issuer; and

²⁶ This section relies heavily on FREDERICK SCHAUER, *PLAYING BY THE RULES: A PHILOSOPHICAL EXAMINATION OF RULE-BASED DECISION-MAKING IN LAW AND IN LIFE* (1991) (hereinafter “PLAYING BY THE RULES”). See also JULIA BLACK, *RULES AND REGULATORS* 6-19 (1997) (hereinafter “BLACK”).

²⁷ Sarbanes-Oxley Act of 2002 § 406(a), 15 U.S.C. § 7264(a) (Supp. III 2003).

(3) compliance with applicable governmental rules and regulations.²⁸

In addition to requiring disclosure about the existence of such a code of ethics, section 406 requires disclosure of any code amendments or waivers. Such disclosure tends to cause companies to adopt a code of ethics since, in the current environment, a public company is rarely prepared to disclose that it has decided against adopting one.

If all stakeholders shared a common view about the effectiveness of corporate codes of ethics, as well as what should be covered by and who should be subject to them, then section 406 would be unnecessary; all companies would have a code (and the right kind of code) without the statute. In fact, however, the effectiveness of codes of ethics has been questioned,²⁹ and people disagree about the appropriate content and application of such codes.³⁰ Indeed, some may dispute the need for *any* code, believing that they and their company are ethical without it; others may differ as to whether particular conduct is or is not ethical. Reputable and well-intentioned individuals and organizations are on all sides of the debate.³¹ Congress concluded, however, that investor confidence in the integrity of the market justified a rule requiring disclosure about codes of ethics. By virtue of the rule, investors and others affected by public companies (including competing companies) need not wonder if a particular company ought to have a code of ethics; the rule effectively requires it.

At the same time, employees do not need the references in section 406 to honest and ethical conduct and to compliance with the law to know that they should not take the company car on a joy-ride at 90 miles an hour on an icy city street, or that the pre-meditated, wanton killing of a colleague is wrong. Forbearance from such activities is often influenced more by the ethical principle underlying the rules – avoiding injury and preserving life are desirable – than by rules that prohibit injuring another person

²⁸ *Id.*

²⁹ See, e.g., Kimberly D. Krawiek, *Cosmetic Compliance and the Failure of Negotiated Governance*, 81 WASH. U. L.Q. 487, 511-12 (2003).

³⁰ See Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002, Securities Act Release No. 33-8177 [2002-2003 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 86,818 at 86,883 (Jan. 23, 2003), at § II.B.2.b, available at <http://www.sec.gov/rules/final/33-8177.htm> (hereinafter “SEC Code of Ethics Release”).

³¹ See Comments on Proposed Rule: Disclosure Required by Sections 404, 406 and 407 of the Sarbanes-Oxley Act of 2002, <http://www.sec.gov/rules/proposed/s74002.shtml>.

intentionally or negligently. That is, that which appears to be rule-governed may actually be norm-governed.³²

In many situations, however, the applicable principle is less clear, or there may be multiple principles at stake, or even well-intentioned people may identify several courses of action that they feel are reasonable ways to give effect to the principle. Rules help us to conduct our affairs in the face of such uncertainties and ambiguities.³³ In these cases, we often are more aware of the rule's requirements than its rationale, but this should not obscure the facts that some principle underlies the rule and that the rule-maker believes that the rule will further the principle. This principle will not be realized, though, if it is simply restated by the rule. Thus, if the purpose of a traffic rule is to improve safety and minimize injuries, then merely requiring drivers to drive safely fails to deal with the many and varying perceptions of what constitutes "safe." Similarly, if the purpose of the code-of-ethics provisions of section 406 is to improve business ethics, then the section would have added nothing had it only required a code directing employees to conduct themselves ethically. To influence conduct, rules must (among other things) require action (or forbearance) that, while consistent with the underlying principle, adds specificity.³⁴

Such specificity has limits, however. Adhering to the speed limit is not the only element of safe driving. The requirements of section 406 are not the only way to achieve more ethical conduct, the officers to whom the specified code applies are not the only employees who should behave ethically, and the behavior included in the statutory definition of "code of ethics" is not the totality of ethical conduct.³⁵ One of the virtues of rules is that they narrow the matters to be addressed. Companies need not deal with all issues that *could* be included in a code, only those that the rule specifies; drivers do not need to consider all aspects of their driving, just their speed. Indeed, more efficient decision-making is fostered precisely because rules encourage us *not* to think of all the possibilities:

³² See Margaret Jane Radin, *Presumptive Positivism and Trivial Cases*, 14 HARV. J. L. & PUB. POL'Y 823, 826 (1991).

³³ See LARRY ALEXANDER & EMILY SHERWIN, *THE RULE OF RULES: MORALITY, RULES, AND THE DILEMMAS OF LAW* 54 (2001) (hereinafter ALEXANDER & SHERWIN").

³⁴ See PLAYING BY THE RULES, *supra* note 26, at 53.

³⁵ Indeed, the SEC added the principal executive officer to the group subject to the code, and required that two additional ethical issues (internal reporting of code violations and accountability for adherence to the code) be covered by the code. Compare Sarbanes-Oxley Act of 2002 § 406(a), 15 U.S.C. § 7264(a) (Supp. III 2003), with SEC Code of Ethics Release, *supra* note 30, §§ II.B.1.b, II.B.2.c.

If we are not to be paralysed by uncertainty, and stumble into numerous errors just because we have too little time to consider too much, we must often simplify our thought processes, using a form of decision-making that limits us to the consideration of a manageable array of factors.

Rules, as we have seen, serve this life-simplifying purpose Rules also serve this agenda-simplifying or desk-clearing function, taking much off the agenda so that what remains can be dealt with with the care and detail it deserves. In this respect, rules have silent virtues, for often we are able to do what we can precisely because rules free us from having to do anything else.³⁶

In the end, we are willing to invest in the capital markets and drive on highways largely because of rules.³⁷

These benefits come at a cost, however. By reducing the range of issues that need to be considered, any rule is rendered incapable of dealing fully with all of the contingencies with which, to further its purpose, the rule might be concerned. When a rule *does not go far enough* – when it fails to prohibit conduct that is inconsistent with its purpose (or does not require conduct that is consistent with its purpose) – it is *under-inclusive*; loopholes are indicative of a rule’s under-inclusiveness. When a rule *goes too far* – when it requires conduct that is inconsistent with its underlying goal – it is over-inclusive;³⁸ a rule requiring detailed disclosures of risks, for example, is over-inclusive (and its purpose is not served) to the extent that such disclosures are unintelligible.³⁹

This over- and under-inclusiveness – “the imperfect match between the rule and its purpose”⁴⁰ – is unavoidable; no amount of careful rule-making will eliminate it.⁴¹ Thus, adjusting the disclosure rule to require a minimum-sized typeface will not prevent a confusing layout, and establishing a maximum speed

³⁶ PLAYING BY THE RULES, *supra* note 26, at 229-30. See also ALEXANDER & SHERWIN, *supra* note 33, at 67.

³⁷ See Linda Meyer, “Nothing We Say Matters”: Teague and New Rules, 61 U. CHI. L. REV. 423, 481 (1994) (“Although the resulting decisions are not perfect, they are better than they would be if the time-pressed, incapable, or untrustworthy decision maker had tried to take all relevant features into account.”).

³⁸ It might seem that a rule is also over-inclusive when it appears to prohibit conduct that is consistent with its purpose. Yet, an act that furthers an ethical purpose more than compliance would (*e.g.*, speeding to take an injured passenger to an emergency room) is generally subject to a justification or excuse defense. See, *e.g.*, Mitchell N. Berman, *Justification and Excuse, Law and Morality*, 53 DUKE L. J. 1, 18-20 (2003). Even the rules governing these defenses exhibit the limitations of rules, however. While they set forth the showing that must be made (and, thereby, eliminate other factors from consideration), they cannot anticipate all justifiable or excusable circumstances, and leave it to the individual to determine and establish that he or she satisfied the applicable standard.

³⁹ See, *e.g.*, Felix G. Rohatyn, *The Financial Scandals and the Demise of the Traditional Investment Banker*, in Lorsch, *supra* note 4, at 135, 136 (“When it comes to underwriting securities and protecting the public, the requirement of ‘full disclosure’ has been superseded by disclosure so massive and detailed that no one but specialists can begin to understand the facts.”).

⁴⁰ BLACK, *supra* note 26, at 8.

⁴¹ See PLAYING BY THE RULES, *supra* note 26, at 50. See also Colin S. Diver, *The Optimal Precision of Administrative Rules*, 93 YALE L. J. 65, 70-71 (1983). The over- and under-inclusiveness that inheres in rules is to be distinguished from the incompleteness that is sometimes deliberately “written into” a rule for reasons of strategy or cost. See Dan M. Kahan, *Ignorance of Law Is an Excuse – But Only for the Virtuous*, 96 MICH. L. REV. 127, 139 (1997).

for radio announcements will not prevent a squeaky-voiced announcement. Alternatively, generalizing the rule so that print or radio disclosure is “intelligible” may not be much help, since each advertiser will be left to determine what is intelligible in its case; some advertisers may make the wrong decision and thereby subject the public to potential harm.

The SEC’s code-of-ethics regulation (section 406) is no different. In adding the principal executive officer to the class of officials subject to the code, the SEC implicitly recognized that the statute’s reach was under-inclusive:

[W]e continue to think that it is appropriate and consistent with the purposes of the Sarbanes-Oxley Act to extend the scope of our rules under Section 406 to include a company’s principal executive officer, as proposed. It seems reasonable to expect that a company would hold its chief executive officer, an official superior to the company’s senior financial officers, to at least the same standards of ethical conduct to which it holds its senior financial officers.⁴²

This expansion made the provision less under-inclusive, but other personnel (*e.g.*, chief operating officers) remain uncovered by the broader regulation. While the SEC must have been concerned about such individuals, it opted to identify particular positions rather than to articulate a more general principle or standard to describe the characteristics of the positions to which the code should apply. As a result, the rule continues to exclude others – whether senior or junior to the specified officers – whose conduct (or misconduct) is as relevant for giving effect to the provision’s purpose.

Rules have the greatest impact when they cause people to behave differently than they would have behaved in the absence of the rule – which is precisely where the rules are over- and under-inclusive. Recall that the average person contemplating a high-speed joy ride or a brutal homicide does not need the legal prohibition to deter him or her from committing the act. By contrast, the speed limit is an important consideration to the driver who must decide how fast to go in inclement weather, and homicide laws are important to the person who has been asked by a terminally ill and pain-ravaged loved one to assist in a suicide. Similarly, section 406 affects the behavior of covered corporate officials less when it requires compliance with applicable laws (which must be adhered to anyway) than when it prohibits conflicts of interest (a standard that is susceptible to over- and under-inclusiveness).

⁴² SEC Code of Ethics Release, *supra* note 30, § II.B.1.b.

RULES AND ETHICAL DECISION-MAKING

In situations where there is no rule or where the rule, because of its over- or under-inclusiveness, is or should be inapplicable, we must look elsewhere for guidance – such as to ethical principles. Our need to consider the ethics of a situation, therefore, arises *because* of rules and, in particular, because of their inherent limitations. Paradoxically, though, these very same attributes interfere with our ability to make and implement ethical decisions.

In the view of many, making and acting on an ethical decision involves (1) recognizing an issue as an ethical one, (2) making an ethical judgment, (3) resolving to do the ethical thing, and (4) actually behaving ethically.⁴³ These steps will be explored below in the context of the rule characteristics discussed above, augmented by descriptions of empirical studies that tend to substantiate the tension between rules and ethical decision-making.

1. Recognizing the Ethical Issue

While the ethical thing to do is often also the legal, economic, or political thing to do, failing to recognize the ethical dimension is not inconsequential. A rule may require something unethical, or there may be no rule at all, or the application of a rule may be unclear. Recognizing the ethical dimension of such situations is important, but may not occur because of (i) the level of our social or cognitive development (young children who cannot comprehend the effect of their act on someone else are absolved of ethical and legal responsibility), (ii) our unawareness that other people are involved, (iii) our distance from the affected people (selling adulterated fruit juice or distributing tainted medical supplies does not raise the same ethical concerns for many people when done in far-away places rather than in their own

⁴³ A number of models have been developed to describe how we make and implement ethical decisions. See Thomas M. Jones, *Ethical Decision Making by Individuals in Organizations: An Issue-Contingent Model*, 16 ACAD. MGMT. REV. 366, 368-72 (1991) (hereinafter “Jones”). This discussion uses the “four component” model developed by James R. Rest (see James R. Rest, *Morality*, in III HANDBOOK OF CHILD PSYCHOLOGY 556, 558-69 (Paul H. Mussen ed., 4th ed. 1983)) because of its relative simplicity and its having served as the basis of still other models (see Jones, *supra*, at 368-72), but acknowledges that the model has not been free from criticism (see, e.g., Gary R. Weaver & Bradley R. Agle, *Religiosity and Ethical Behavior in Organizations: A Symbolic Interactionist Perspective*, 27 ACAD. MGMT. REV. 77, 82 (2002)).

country⁴⁴), or (iv) the deliberate minimizing of an act's impact on potential victims (e.g., the military's de-personalization of the enemy to ease ethical qualms of combat trainees⁴⁵).

Experiments have confirmed that acting ethically depends on the extent to which we are (or feel) close to the victim/beneficiary of our action. Stanley Milgram demonstrated that people's willingness to follow orders and give what they believed were increasingly strong electric shocks to others decreased as the physical and acoustical separation between subject and "victim" decreased.⁴⁶ A more recent experiment used a magnetic resonance imager (MRI) to monitor brain activity as subjects considered a series of personal and impersonal moral dilemmas.⁴⁷ Brain scans revealed that those areas of the brain associated with emotion were more active when the moral-personal dilemmas were considered than when the moral-impersonal ones were considered; subjects felt more connected to the victim in the former cases than in the latter ones. The study's author noted the correlation between the salience of the other person and our ability to recognize the moral dimension of a situation:

[W]e ignore the plight of the world's poorest people not because we implicitly appreciate the nuanced structure of moral obligations, but because, the way our brains are wired up, needy people who are "up close and personal" push our emotional buttons, whereas those who are out of sight languish out of mind.⁴⁸

While the ease and speed with which we become engaged with the victim or beneficiary of our act are important in recognizing the ethical nature of a situation, rules make that engagement more difficult and slower. Rules shift our attention from a broad goal or purpose to a particular way of achieving it – from general traffic safety to speed limits, from good corporate governance to codes of ethics on specific subjects applicable to particular officers. But as they narrow our focus, rules divert our attention *away*

⁴⁴ See Walt Bogdanich & Eric Koli, *2 Paths of Bayer Drug in 80's: Riskier One Steered Overseas*, N.Y. TIMES, May 23, 2003, at A1. See also David M. Messick & Max H. Bazerman, *Ethical Leadership and the Psychology of Decision Making*, 37 SLOAN MGMT. REV. 9, 15-16 (1996).

⁴⁵ See Dan Baum, *The Price of Valor*, NEW YORKER, July 12 & 19, 2004, at 44, 46.

⁴⁶ See STANLEY MILGRAM, OBEDIENCE TO AUTHORITY: AN EXPERIMENTAL VIEW 32-43 (1974) (hereinafter "MILGRAM").

⁴⁷ See Joshua Greene et al., *An fMRI Investigation of Emotional Engagement in Moral Judgment*, 293 SCIENCE 2105 (2001). A personal dilemma would include such situations as throwing someone from a lifeboat; an impersonal one would include scenarios such as finding someone's lost wallet.

⁴⁸ Joshua Greene, *From neural "is" to moral "ought": what are the moral implications of neuroscientific moral psychology?*, 4 NEUROSCIENCE 847, 849 (2003).

from other people.⁴⁹ We become less aware of others and more aware of our own compliance (or non-compliance) with the rule:

First, legalistic remedies can erode the interpersonal foundations of a relationship they are intended to bolster because they replace reliance on an individual's "good will" with objective, formal requirements. . . .

Second, when rules and procedures form the basis of continuing relations they can disrupt the "implicit agreements" that efficiently govern social interaction by interposing a structural barrier between the parties, making the relationship feel less direct and close.⁵⁰

Rule-makers *do not want* us to make *ad hoc* decisions and, as noted, one of the advantages of rules is the efficiency and energy conservation that results from decisions being made for us. In inclement conditions, we do not need to think about whether driving at the speed limit will harm others (or ourselves), since adhering to the limit is, by definition, "safe."⁵¹ And if we exceed the speed limit (or consider doing so), our concern is much less on whether speeding will endanger *them*, and much more on whether the trooper will pull *us* over. To the extent that a rule causes us to focus on whether we are adhering to it (or will get caught for not adhering to it), rather than on how our conduct will affect others, we are more likely to gloss over or altogether miss the situation's ethical dimension.⁵²

In an *ideal world*, one where rules are unnecessary, we could be counted on to decide safety issues correctly in light of our own skill, road conditions, and various other factors. In the *real world* – the one with rules, including speed limits – rule-makers have decided for us what kind of conduct constitutes safe driving, and our focus shifts (quite literally) from others on the highway to our own speedometer.⁵³

⁴⁹ See, e.g., Ben Hamilton-Baillie, *Urban Design: Why Don't We Do It in the Road? Modifying Traffic Behavior through Legible Urban Design*, 11 J. URBAN TECH. 43, 55 (2004) (hereinafter "Hamilton Baillie") ("Many measures intended to improve safety have the effect of divorcing the driver from the need to interact with people and with their surroundings."). See also discussion accompanying notes 54, 55.

⁵⁰ Sim B. Sitkin & Nancy L. Roth, *Explaining the Limited Effectiveness of Legalistic "Remedies" for Trust/Distrust*, 4 ORG. SCI. 367, 376 (1993) (citation omitted).

⁵¹ Cf. JOHN G. KEMENY ET AL., REPORT OF THE PRESIDENT'S COMMISSION ON THE ACCIDENT AT THREE MILE ISLAND 9 (1979), available at http://www.pddoc.com/tmi2/kemeny/attitudes_and_practices.htm ("[R]egulations alone cannot assure safety. Indeed, once regulations become as voluminous and complex as those regulations now in place, they can serve as a negative factor in nuclear safety. . . . The satisfaction of regulatory requirements is equated with safety.").

⁵² See Marc D. Street et al., *The Impact of Cognitive Expenditure on the Ethical Decision-Making Process: The Cognitive Elaboration Model*, 86 ORG. BEHAVIOR AND HUMAN DECISION PROCESSES 256, 270 (2001) ("[I]t is not overly cynical to assert that many individuals make decisions on the basis of how the outcomes affect themselves while simultaneously giving little regard to how they impact others.").

⁵³ Admittedly, rules may universalize: everyone must obey the speed limit, not only me and not only the driver next to me. This is not inconsistent with the narrowing tendency of rules since the universalizing and narrowing occur in different contexts; I am not called upon to make ethical decisions with respect to

Somewhere between the *real world* and the *ideal world* is the space in which Hans Monderman works.

Monderman is a Dutch traffic engineer who has improved traffic safety by eliminating the rules of the road:

To make communities safer and more appealing, Mr. Monderman argues, you should first remove the traditional paraphernalia of their roads – the traffic lights and speed signs; the signs exhorting drivers to stop, slow down and merge; the center lines separating lanes from one another; even the speed bumps, speed-limit signs, bicycle lanes and pedestrian crossings. In his view, it is only when the road is made more dangerous, when drivers stop looking at signs and start looking at other people, that driving becomes safer.

“All those signs are saying to cars, ‘This is your space, and we have organized your behavior so that as long as you behave this way, nothing can happen to you,’” Mr. Monderman said. “That is the wrong story.”⁵⁴

Monderman’s approach “is increasingly seen as the way of the future in Europe.”⁵⁵ No claim is being made here that traffic rules should be abandoned, or that they serve no purpose (or even that they do more harm than good). Indeed, it is doubtful that the success of eliminating traffic rules in small European towns could be replicated in large metropolitan areas. At the same time, it behooves us to acknowledge that, for all their virtues, rules (and not only traffic rules) have vices as well.

The corporate response to recent scandals also shows this limiting tendency of rules. Despite the public’s need for reassurance about business values and culture, business itself is focused much more on rule compliance. One recent international survey of senior executives in financial institutions concluded “that governance is equated in many cases with meeting the demands placed on institutions by regulators and legislators, not with taking proactive steps to determine what it is that customers want over and above the minimum standards set down by regulators and thereby giving themselves a strategic advantage”⁵⁶

Some might argue that we remain aware of the impact of our conduct even when we engage in or contemplate more extreme rule deviations. In support, they would assert that, since we do not drive cars as fast as they can go on deserted highways where no police lurk, we must still be concerned, not simply with rule compliance, but also with safety more generally. Even aside from the fact that the only risk of injury is

those who drive on highways the day after I do, or who drive at the same time but on the other side of the state.

⁵⁴ Sarah Lyall, *A Path to Road Safety With No Signposts*, N.Y. TIMES, Jan. 22, 2005, at A4 (hereinafter “Lyall”). See also Hamilton-Baillie, *supra* note 49, at 56.

⁵⁵ Lyall, *supra* note 54. See also Malcolm Gladwell, *Blowup*, NEW YORKER, Jan. 22, 1996, at 32, 36 (“Why are more pedestrians killed crossing the street at marked crosswalks than at unmarked crosswalks? Because they compensate for the ‘safe’ environment of a marked crossing by being less vigilant about oncoming traffic.”).

⁵⁶ See PricewaterhouseCoopers & Economist Intelligence Unit, *Governance: From Compliance to Strategic Advantage* 3 (2004), <http://www.pwc.com/images/gx/eng/fs/0404eiugov.pdf>.

to ourselves if the highway is deserted, the practical issue is not whether awareness of and concern for others (*e.g.*, the impact on surviving family members, the cost to society) may *linger* at the edges despite the rules, but that rules *weaken* such awareness and concern. This weakening will have a far greater impact on conduct that is closer to the compliance–noncompliance line (and therefore more likely and foreseeable) than on more extreme conduct.

Sanctions – that which distinguishes a rule from a suggestion – affect how we see the dilemma, which also has important implications for ethical recognition. In an intriguing experiment that probed the effect of sanctions, MBA students were provided with a scenario in which they were faced with a choice between agreeing to limit toxic emissions voluntarily and facing onerous regulation.⁵⁷ The issue of whether to comply with the voluntary agreement (no penalty for a violation) was characterized as an “ethical” one by 55.2 percent of the respondents but as a “business” (economic) one by 44.8 percent. When non-compliance involved even weak sanctions, however, respondents viewing the issue as “ethical” decreased to 19.2 percent, while those viewing it as a “business” decision increased to 76.9 percent. Thus, the presence or absence of sanctions (and, by extension, the existence of a rule) affected whether or not the issue was recognized as an ethical one:

Results revealed that the presence of weak sanctions promoted a focus on the business aspects of the decision in contrast to a focus on the ethical aspects when no sanctions were present. The [students’] written comments further support the notion that a weak sanctioning system prompts a perception that the decision concerns the costs versus the benefits of cooperating, whereas the lack of such a system prompts relatively more consideration of the ethical aspects of the decision.⁵⁸

Finally, an issue has an ethical dimension only if the decision-maker has volition, and rules eliminate (or at least reduce) our choice. In this sense, a rule against feeding animals at the zoo has a greater impact than the law against murder because, while most people would not murder if there were no such legal prohibition,⁵⁹ many people would choose to feed the animals if doing so were not prohibited. Any rule that leaves the zoo visitors feeling that they still have a choice is ineffective. The distinction here is not in the *importance* of the rule’s content (murder *is* more important than not feeding zoo animals), but in the *nature* of the content and, specifically, in the degree to which the rule itself actually affects our

⁵⁷ Ann E. Tenbrunsel & David M. Messick, *Sanctioning Systems, Decision Frames, and Cooperation*, 44 ADMIN. SCI. Q. 684 (1999).

⁵⁸ *Id.* at 697-98.

⁵⁹ See Tom R. Tyler & John M. Darley, *Building a Law-Abiding Society: Taking Public Views About Morality and the Legitimacy of Legal Authorities Into Account When Formulating Substantive Law*, 28 HOFSTRA L. REV. 707, 716 (2000).

behavior. Strong rules are those that actually eliminate the decision (choice) we may have made if the rule did not exist.⁶⁰ Since an issue is an ethical one only when we have the freedom to choose, the elimination of choice diminishes our ability to recognize the ethical nature of an issue.

It might be argued in response that rules do not preclude us from choosing to focus on related considerations of an ethical nature. Thus, a prohibition against feeding the animals does not prevent people interested in animal welfare from donating funds to enable the zoo to purchase goods or services to benefit the animals; Sarbanes-Oxley does not require public companies to publish their codes of ethics in the popular press, but companies are free to do so; businesses do not seem to be required to air radio advertisements with disclaimers spoken slowly enough to be understood, but they are free to do so; and so on. Yet, such conduct is possible only if those subject to the rule are aware of those possibilities in the first place. If they are not, then the freedom to choose that course is essentially non-existent.⁶¹

2. Making the Ethical Judgment

Ethical dilemmas require ethical responses. While generally agreeing that the process of formulating a response (or considering whether someone else's response is ethical) is a cognitive one,⁶² experts disagree about its nature and, in particular, about the role of reason in this process. Some believe that moral judgments are reached by a deliberate and conscious reasoning process, and that the reasons we use to make ethical decisions evolve as we develop and mature. Lawrence Kohlberg explained that this evolution involved moving from the "pre-conventional" level (where "right" is what is in our self-interest) to the "conventional" level (where "right" is fulfilling the expectations of others and upholding laws and the social system), to the "post-conventional" level (where "right" is not limited to laws, but includes – and ultimately rests on – higher ethical principles).⁶³

⁶⁰ See Owen D. Jones & Timothy H. Goldsmith, *Law and Behavioral Biology*, 105 COLUM. L. REV. 405, 499 (2005); PLAYING BY THE RULES, *supra* note 26, at 104.

⁶¹ The concern here is less how much choice (and freedom to violate the rule) the decision-maker *actually* has in the face of the rule, and more the degree of choice and freedom that the decision-maker *feels* that he or she has. Cf. PLAYING BY THE RULES, *supra* note 26, at 9 ("A rule giving the addressee a choice whether to comply or not but rewarding compliance with payment of one million dollars is a rule in which the formal option is in practice unavailable." (footnote omitted)).

⁶² See Jonathan Haidt, *The Emotional Dog and Its Rational Tail: A Social Intuitionist Approach to Moral Judgment*, 108 PSYCH. REV. 814, 818 (2001) (hereinafter "Haidt").

⁶³ See, e.g., Lawrence Kohlberg, *Moral Stages and Moralization: The Cognitive-Developmental Approach*, in MORAL DEVELOPMENT AND BEHAVIOR: THEORY, RESEARCH, AND SOCIAL ISSUES 31 (Thomas Lickona ed., 1976) (hereinafter "Kohlberg/Lickona").

Others hold that, when confronted by an ethical issue, we do not reason to a conclusion; we “simply” and spontaneously know the answer intuitively.⁶⁴ The ways in which our intuition develops is well beyond the scope of this article; for present purposes, it suffices to note that reason plays a role also in the social intuitionist model. The distinction has been analogized to the different ways that judges (or scientists) and lawyers use reason: whereas the former employ reason to identify truth, the latter use it to support whatever argument has already been decided to be in the client’s best interest.⁶⁵

Despite their fundamental differences, the two models have much in common. Whatever the basis of our ethical judgment – reason or reason-influenced intuition – more developed reasoning or intuition (as the case may be) affects the actual judgment we make, not just the way we reach it. Social interaction plays a crucial role in the refinement of both reasoning and intuition. Compare:

Kohlberg: “Moral development depends upon stimulation defined in cognitive-structural terms, but this stimulation must also be social, the kind that comes from social interaction and from moral decision-making, moral dialogue, and moral interaction.”⁶⁶

Haidt: “By seeking out discourse partners who are respected for their wisdom and open-mindedness, and by talking about the evidence, justifications, and mitigating factors involved in a potential moral violation, people can help trigger a variety of conflicting intuitions in each other. If more conflicting intuitions are triggered, the final judgment is likely to be more nuanced and ultimately more reasonable.”⁶⁷

Indeed (and as evidence of the degree of overlap between the two models), Haidt suggests that Kohlberg’s tool for improving moral judgment can also be effective in the social intuitionist model:

Kohlberg created an environment where students and teachers enacted equality. Years of such implicit learning, coupled with explicit discussion, should gradually tune up intuitions about justice, rights and fairness, leading perhaps to an automatic tendency to look at problems from multiple perspectives. By creating a community in which moral talk was ubiquitous . . . and in which adults modeled good moral thinking, Kohlberg may well have strengthened his students’ tendency to use . . . private reflection on their own.”⁶⁸

This similarity between the two models points to the way that rules may impede moral judgment – or, more precisely, may impede the process of improving our moral judgment. Better judgment is

⁶⁴ Haidt, *supra* note 62, at 818.

⁶⁵ *Id.* at 828-29. This view is consistent with the emerging awareness that the thought process in which human beings engage generally (not only about ethical issues) functions on dual levels – one that “is rapid, intuitive, but sometimes error-prone [and another that] is slower, reflective, and more statistical.” Cass R. Sunstein, *Hazardous Heuristics*, 70 U. CHI. L. REV. 751, 754 (2003) (reviewing HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT (Thomas Gilovich et al. eds., 2002)) (hereinafter “Sunstein, *Hazardous Heuristics*”). See also ANTONIO DOMASIO, DESCARTES’ ERROR: EMOTION, REASON, AND THE HUMAN BRAIN 189 (1994).

⁶⁶ Kohlberg/Lickona, *supra* note 63, at 49.

⁶⁷ Haidt, *supra* note 62, at 829.

⁶⁸ *Id.* (citations omitted).

promoted by stretching people, exposing them to different and conflicting viewpoints and approaches to problem-solving.⁶⁹ The problem is that rules set forth “minimum conditions [and are not] designed to bring about higher levels of aspiration”⁷⁰ They fail to “unleash much moral imagination or commitment [or to] inspire human excellence or distinction.”⁷¹ By their very nature, rules (and rule-based ethics training) play to our “comfort zone,” and fail to spur us to more sophisticated approaches to ethical decision-making.

3. Resolving to Do the Ethical Thing

Once we determine an ethical response, we must take the next step, and accord it the highest priority among all alternative courses of action. Doing so successfully depends on how we perceive ourselves and the importance we attach to ethical values.

Autonomy

Most parents have had the experience of suggesting that a small child play with Toy A rather than Toy B – only to have the child then insist on playing with Toy B. From an early age, human beings crave autonomy, and when it is eliminated or threatened, they often try to restore it by acting in direct opposition to the threatened constraint, a process known as “psychological reactance.”⁷² A survey of nearly 3,400 students on 56 campuses throughout the country revealed that underage drinking actually *increased* after a number of states raised the legal drinking age to 21.⁷³ Reactance theory suggests that, even if students did not actually drink on campus or purchase alcohol before 1987, they had been free to do so if they wished. When the law was changed, this freedom was taken away – prompting underage students to assert themselves by doing what the new law now prohibited them from doing.

Reactance might be invoked to argue that – at least with regard to those rules whose requirements are aligned with ethical conduct – rules undermine ethical behavior by prompting people to act contrary to

⁶⁹ See, e.g., THOMAS R. PIPER ET AL., CAN ETHICS BE TAUGHT? PERSPECTIVES, CHALLENGES, AND APPROACHES AT HARVARD BUSINESS SCHOOL 52 (1993).

⁷⁰ BARDACH & KAGAN, *supra* note 19, at 100.

⁷¹ Paine, *supra* note 15, at 111.

⁷² See generally SHARON S. BREHM & JACK W. BREHM, PSYCHOLOGICAL REACTANCE: A THEORY OF FREEDOM AND CONTROL (1981). See also IRVING L. JANIS & LEON MANN, DECISION MAKING: A PSYCHOLOGICAL ANALYSIS OF CONFLICT, CHOICE, AND COMMITMENT 256-58 (1977); Robert A. Kagan & John T. Scholz, *The “Criminology of the Corporation” and Regulatory Enforcement Strategies*, in ENFORCING REGULATION 67, 73-74 (Keith Hawkins & John M. Thomas eds., 1984) (hereinafter “Kagan & Scholz”).

⁷³ See Ruth C. Engs & David J. Hanson, *Reactance Theory: A Test With Collegiate Drinking*, 64 PSYCH. REP. 1083 (1989).

them. There are two rejoinders to such an argument. First, the starting point for reactance is our freedom to do (or refrain from doing) something – whether or not we actually do (or refrain from doing) it. That freedom gives us our sense of autonomy. The autonomy is eliminated when a rule takes or threatens to take away that freedom. This differs from the scenario where restrictions have already been in place. Teenagers who turn 16 these days, for example, are not (and were never) legally able to drink or to purchase alcohol. Thus, reactance cannot explain behavior contrary to the universe of long-extant rules. Second, re-establishing one’s autonomy by violating rules does not necessarily lead to unethical behavior. A student may get seriously drunk and then drive a car; but he or she might illegally take only one drink and go to bed. Putting aside the issue of whether violating any rule to any extent is unethical, the point is that one can reassert autonomy in various ways, including ways that many people would not deem unethical.

At the same time, reactance theory should not be dismissed too hastily. First, as has been shown, rules are most powerful precisely where they prompt us to act (or not act) differently than we would without them. If we are not inclined to speed or commit murder, rules prohibiting such activities would not threaten our autonomy. If we are tempted to jaywalk, on the other hand, the prohibition impinges on our freedom to do so and, in that sense, has force even though such conduct may long have been illegal. Explaining (or excusing) a rule violation on the basis that “No one is going to tell me what I can or cannot do” – which captures the crux of reactance – is not limited to new rules. Second, reactance can color our view of and confidence in the effectiveness of rules and regulations generally. A study undertaken shortly after Miami banned the use of detergents containing phosphates found that, compared to residents of a city without such a regulation, Miami residents were less optimistic that regulatory action would solve the water pollution problem.⁷⁴ Diminished respect for rule-makers or faith in the rule-making process, of course, is a frequently heard explanation for rule violations.

Overjustification

Whereas psychological reactance does not always interfere with good conduct (sometimes it does not apply, and at other times violations do not constitute unethical behavior), a more serious risk to decision-making is posed by over-justification, the concept “that people’s intrinsic interest in an activity

⁷⁴ See Michael B. Mazis, *Antipollution Measures and Psychological Reactance Theory: A Field Experiment*, 31 J. PERSONALITY & SOC. PSYCH. 654, 657 (1975).

will be decreased to the extent that the performance of that activity, heretofore attributed to internal causes, is reattributed to external causes.”⁷⁵ Over-justification is most often invoked to explain situations in which individuals, initially internally motivated to engage in some activity (studying, helping another person), lose their interest in doing so after a reward for performing that activity is introduced and then removed.⁷⁶ Over-justification has also been used to explain situations in which (i) external coercion *to do* something pleasant (imposing deadlines on a game) *decreased* interest once the deadlines were removed,⁷⁷ and (ii) external threats *not to do* something fun (play with a desirable toy) *increased* interest in the activity later.⁷⁸

These contexts involve attractive activities. Rules, however, are essentially external motivators to avoid doing something society deems undesirable (speeding, disclosing inaccurately). Thus, external threats imposed to prevent people from doing something that they may already be internally motivated to *avoid* are relevant. Studies of over-justification in this setting are much rarer than those involving rewards, even though such threats may have a greater impact on intrinsic motivation than rewards (which the intended recipient has greater freedom to accept or reject).⁷⁹ Nonetheless, experiments have shown that interest in an unattractive activity actually *increased* in the face of threats to avoid the activity.⁸⁰

In one study, college students were directed to complete an inconsequential trivia questionnaire. They were told that a proctor would not be present in the room but that, because prior test-takers had been interested in the answers, those answers were written on the blackboard but obscured from view. One-third of the students were also told not to look at the answers until the proctor returned, one-third were given a more severe threat (if they looked at the answers, they would ruin the experiment and would not be given credit for participating in the study), and one-third were given no additional instructions. Students were observed through a one-way mirror as they took the test. None of them – not even those who had been given no instructions about looking at the answers – attempted to look at those answers; this confirmed that

⁷⁵ G. Daniel Lassiter, *Effect of Superfluous Deterrence on the Perception of Others*, 22 J. EXPERIMENTAL SOC. PSYCH. 163 (1986) (hereinafter “Lassiter”). See also Timothy F. Malloy, *Regulation, Compliance and the Firm*, 76 TEMP. L. REV. 451, 522 (2003) (hereinafter “Malloy”).

⁷⁶ See, e.g., Edward L. Deci et al., *A Meta-Analytic Review of Experiments Examining the Effects of Extrinsic Rewards on Intrinsic Motivation*, 125 PSYCH. BULL. 627, 630 (1999).

⁷⁷ See, e.g., Teresa M. Amabile et al., *Effects of Externally Imposed Deadlines on Subsequent Intrinsic Motivation*, 34 J. PERSONALITY AND SOC. PSYCH. 92 (1976).

⁷⁸ See Timothy D. Wilson & G. Daniel Lassiter, *Increasing Intrinsic Interest With Superfluous Extrinsic Constraints*, 42 J. PERSONALITY AND SOC. PSYCH. 811, 812 (1982) (hereinafter “Wilson & Lassiter”).

⁷⁹ See BRUNO S. FREY, NOT JUST FOR THE MONEY: AN ECONOMIC THEORY OF PERSONAL MOTIVATION 30 (1997) (hereinafter “FREY”).

⁸⁰ See Wilson & Lassiter, *supra* note 78; Lassiter, *supra* note 75.

everyone viewed cheating as intrinsically unattractive. After the questionnaires were completed, the proctor returned, and made the answers available.

As part of the same study, the students took a second test several days later without being informed of any connection between the tests. This test was a challenging achievement test, creating a greater incentive to perform well. Students were told that they would take the test unsupervised, and that they needed to answer eight questions sequentially, that they could not spend more than one minute on each question and that, once they proceeded to the next question, they could not return to an earlier one for any reason. No threats were issued. The students were again observed through a one-way mirror to determine if they cheated, *i.e.*, if they reviewed and/or reworked an earlier question despite clear directions to the contrary.

Unlike with the first test, cheating did occur on the second test. The study's focus was not on why students cheated on the second test but not on the first (after all, the first test was a series of inconsequential trivia questions, whereas the second test was more achievement-oriented); rather, the experimenters wanted to determine if, despite the *intrinsic* unattractiveness of cheating (established by the fact that no one cheated on the first test), conduct on the second test was affected by *extrinsic* factors present in the first test. In fact, there *was* a striking correlation between cheating and whether, in the initial test, the student had been in the "mild threat," "severe threat," or "no threat" group. Students who, in the first test, had received the severe threat did the most cheating, followed by those who had received the mild threat, followed by those who had received no threat. Even more telling, after the second test (and disclosure of its relation to the first test), students were asked why they did not cheat on the *first* test (recall that no one cheated on that one); students who had received a severe threat attributed their not cheating to the threat; those who had not been threatened stated that they did not cheat because of intrinsic values; those who had received weak threats were in between. The study's authors concluded that the threat diminished the role of internal values in guiding the students' conduct:

[S]uperfluous threats not to cheat in one situation increased the likelihood that subjects would cheat in a subsequent, constraint-free situation. Subjects who received threats downplayed intrinsic reasons not to cheat, that is, they appear to have discounted their own honesty as a reason why they did not look at the answers at Session 1, which caused them to cheat more at Session 2.⁸¹

⁸¹ Wilson & Lassiter, *supra* note 78, at 817.

Not only can external factors diminish intrinsic values, but they can also prompt undesirable behavior:

“[S]urveilled employees, who may now conceive of themselves as less honest, should be more willing to attempt to trick or bypass the surveillance system, sending supervisors scurrying to find even more sophisticated (and expensive) control systems.”⁸²

Threats directed to potential cheaters or shoplifters are no different than ones directed to potential fraudulent accountants, inaccurate disclosers, and other business miscreants. Indeed, business conduct has been explained in part on the basis of the effect of external factors on internal values.⁸³ Moreover, there is no material difference between prohibitions and prescriptive rules in this context since the threat of punishment will be realized either if one does the prohibited act or fails to do the required act. Before over-justification can be extended to the relationship between rules and intention, however, one clarification is in order. Typically, the over-justification theory is concerned with the effect of behavior when the external reward or constraint is removed. When people are rewarded for something they otherwise enjoy and the reward is then withdrawn, their interest in the act may wane; when students are threatened with consequences if they cheat and the threats are later removed, those previously uninterested in cheating may be more likely to cheat. With rules, a different dynamic applies: once laws and regulations are put in place, they almost always remain in effect (although they may be modified at some point). Most roads have speed limits, even if the maximum speed is adjusted from time to time; similarly, *some* form of accounting and disclosure rules will continue to exist. As long as the rule remains in effect – the external factor continuing to exert its constraining influence – then one might suppose that there should be no lapse in motivation. That is, it would not matter if intrinsic motivation declined (or, more precisely, one would not have occasion to notice any such diminution) since the external motivation would remain constant.

This qualification does not affect the relevance of over-justification to this inquiry. Superfluous rewards or constraints affect perception. People see themselves (and are seen by others) as being motivated by the reward or the threat rather than by intrinsic factors (*e.g.*, preferences, values). In some other class,

⁸² Robert B. Cialdini, *Social Influence and the Triple Tumor Structure of Organizational Dishonesty*, in CODES OF CONDUCT: BEHAVIORAL RESEARCH INTO BUSINESS ETHICS 44, 57 (David M. Messick & Ann E. Tenbrunsel eds., 1996) (hereinafter “Cialdini”). See also Lassiter, *supra* note 75, at 172.

⁸³ See Cialdini, *supra* note 82, at 57; John Braithwaite, *Rewards and Regulation*, 29 J. LAW & SOC’Y, 12, 16 (2002); Mark R. Lepper, *Social-Control Processes and the Internalization of Social Values: An Attributional Perspective*, in SOCIAL COGNITION AND SOCIAL DEVELOPMENT: A SOCIOCULTURAL PERSPECTIVE 294, 297 (E. Tory Higgins et al. eds., 1983).

the students would have sat for a test and not been threatened with sanctions for cheating. At *that* time per the theory, their conduct would have been affected by the *then*-absence of threats, as well as their self-perception (based on their earlier experience) that they are motivated by threats rather than by their own value system. This is illustrated by studies of residents in old-age homes who were given tokens (redeemable at the institutional “store”) for performing certain tasks such as making their beds and cleaning their rooms: rather than motivating the residents to care for themselves generally, the practice caused the residents to *abdicate* their responsibility for all tasks for which they did not receive tokens.⁸⁴

The effect of rules is no different. Few would take issue with the desirability of good corporate governance or candid communications with customers and the general public. If corporate governance or communication with customers and the public is motivated by extrinsic factors such as the requirements of Sarbanes-Oxley or the penalties for incomplete (though well-intentioned) disclosure, the intrinsic drivers – the inherent desirability of good governance and candid communication – may diminish in importance.⁸⁵ Indeed, managers may see themselves and be seen by others as reacting to rules more generally rather than to their own (consistent) feelings. This would be harmless if rules addressed all contingencies. As we have seen, however, rules are over- and under-inclusive where they do exist – and they do not exist for all situations in any event.

4. Acting Ethically

To be ethical, our *intention* to do the ethical thing must be followed by our really *doing* it. Thus, individuals who, despite the negative pull exerted by rules, have recognized an ethical issue, decided on an ethical response, and resolved to act on it, still need to contend with pressures and other obstacles that interfere with actually implementing their decision. Among the varied impediments that must be overcome even at this late stage are – once again – the rules themselves. In the context of this inquiry, implementing an ethical decision will not be materially affected by rules where following the rule also achieves the ethical result. While compliance with the rule may be difficult due to the rule’s vagueness or complexity,⁸⁶ the rule is unlikely to be an obstacle to doing the right thing since the decision-maker has already resolved

⁸⁴ See FREY, *supra* note 79, at 16.

⁸⁵ See IAN AYRES & JOHN BRAITHWAITE, RESPONSIVE REGULATION: TRANSCENDING THE DEREGULATION DEBATE 49 (1992) (“[T]he less salient and powerful the control technique used to secure compliance, the more likely that internalization will result.” (citations omitted)).

⁸⁶ See Malloy, *supra* note 75, at 487.

to do the ethical thing. Where that result would follow from complying with the rule anyway, it is difficult to see how the nature of rules would cause the decision-maker to stray from that desirable path.

There are many instances where “legal” does not equate with “ethical,” however. There may not be a rule covering the situation at hand, there may be a general rule that is inapplicable (or should not be applied) to the situation, or a rule may apply but, substantively, would require unethical behavior. The issue is whether, in such circumstances, rules make it more difficult for the well-intentioned decision-maker to implement his or her decision.

The fewer the obstacles and the easier it is to implement an intention, the greater the likelihood that it will actually be implemented. The reality is that business presents a host of obstacles:

All other things equal, most [business people] would unhesitatingly choose the high road. But, except in hypothetical situations, all other things are never equal. And we often see that factors with more motivational punch – sales quotas, corporate financial health and survival, competitive concerns, career advancement – outweigh ethical choices in business decisions.⁸⁷

To this list, one might add such organizational influences as peer pressure and “group-think,” diffused decision-making structures and dispersed information, compensation, promotion, and other policies that motivate certain behavior – as well as individual factors, including personality and the stage of one’s moral development.⁸⁸

Rules should not be blamed for these influences, which arise and exist independent of rules. Yet, rules, themselves, *are* an obstacle to implementing ethical decisions. Sometimes they are so numerous or complex that employees do not understand them or how to comply with them.⁸⁹ These aspects of rules will not be pursued here, though, because this article undertook to analyze the effect on behavior of rule *nature* rather than *content*, and rules are not inherently complex or numerous. There are several characteristics of rules, however, that *do* affect the implementation of decisions.

Rules have been described as having “clear edges.”⁹⁰ Even where their language is imprecise or vague, they generally are more specific and directive than ethical principles. As a result, variation in the

⁸⁷ Cialdini, *supra* note 82, at 51. See also Maurice E. Schweitzer et al., *Goal Setting as a Motivator of Unethical Behavior*, 47 ACAD. MGMT. J. 422 (2004).

⁸⁸ See, e.g., LINDA KLEBE TREVIÑO & GARY R. WEAVER, *MANAGING ETHICS IN BUSINESS ORGANIZATIONS* 174-81 (2003).

⁸⁹ See, e.g., CHRISTOPHER STONE, *WHERE THE LAW ENDS: THE SOCIAL CONTROL OF CORPORATE BEHAVIOR* 101 (1975) (“The very creation of a huge, cumbersome network of rules may make those subject to them abdicate their independent responsible judgment . . .”).

⁹⁰ Cass R. Sunstein, *Problems With Rules*, 83 CAL. L. REV. 953, 995 (1995).

interpretation of rules (as a class) is narrower than with principles (as a class). People are more comfortable with, and therefore more likely to grab onto, a tangible rule than an amorphous ethical principle whose application to a particular situation is unclear. This is particularly true in pressured environments, such as business situations:

At precisely those moments when mindful awareness and action are most crucial – to discern and address ethical considerations – people are even more likely to stray into wrongdoing. When performance pressures heighten and conflicts among a variety of considerations intensify, people emit their dominant responses, conducting themselves according to their most accustomed behaviors. Instead of meeting ethical challenges with the necessary cognitive and behavioral resources, people retreat into comfortable and familiar patterns of behavior, inadequate in addressing the complex situations they face.⁹¹

Because the requirements of rules are generally clearer than those of ethical principles, violations can be detected more easily and more quickly. For example, determining that a code of ethics has failed to include certain specified topics can be made more readily than determining that the code does not quite reflect the right sense of values. The consequences of violations also differ, with rule violations leading to discipline such as fines, termination, and imprisonment, and principle violations leading to guilt or shame. For these reasons, people are more likely to avoid rule violations rather than breaches of ethical principles:

[A]t least for the great mass of individuals in modern industrialized nations, the disutility due to losing one's entire wealth or of going to jail for life outweighs, and probably by a significant amount, the sting of guilt and of disapproval, or rather that plus the utility from virtue and praise.⁹²

This tendency is particularly powerful because rules provide a basis for deflecting criticism for one's actions. The employee who follows the rule despite a conflicting ethical interest is able to point to the requirements of the rule, and can claim that he or she really did not have a choice. The employee does not have the option of shifting "blame" to the rule-maker when his or her ethically motivated conduct is not legally required and someone else (*e.g.*, the employee's manager) has another view of the ethics of the situation.⁹³ This is especially difficult if a rule applied and dictated a contrary result.

Not only do rules enable us to deflect criticism, but rules also provide a shield against regulatory actions, prosecutions, and civil lawsuits. Unquestionably, the predictability afforded by rules – the knowledge of what constitutes a violation – is one of the virtues of rules. At the same time, however, the

⁹¹ Joshua D. Margolis, *Psychological Pragmatism and the Imperative of Aims: A New Approach for Business Ethics*, 8 BUS. ETHICS Q. 409, 413 (1998) (citations omitted). See also KARL E. WEICK, MAKING SENSE OF THE ORGANIZATION 110 (2001); Kagan & Scholz, *supra* note 72, at 82 (citation omitted).

⁹² Shavell, *supra* note 21, at 236.

⁹³ See, *e.g.*, PLAYING BY THE RULES, *supra* note 26, at 153.

quest for clarity can discourage ethical action that would go beyond legal requirements and possibly create legal exposure. It remains to be seen, for example, whether the Sarbanes-Oxley code-of-ethics provisions, themselves, will achieve their intended purpose, or whether more tangible and immediate pressures will prevail. There is already speculation that mandated public disclosure of code waivers – prompted by the post-Enron focus on transparency on this subject – may actually prompt firms to adopt the narrowest possible codes that still satisfy the legal requirements.⁹⁴ A narrow code will minimize the need for waivers; but it will also prohibit fewer activities, perhaps even fewer than codes had disallowed before the new requirements.⁹⁵ The worthiness of a broad code of ethics – something that the SEC has even urged⁹⁶ – may yield to concerns about whether a code that is broader than required will increase the company’s exposure.

IMPLICATIONS

Once the effect of rules on ethical decision-making is recognized, it follows that rules cannot be the exclusive solution to ethical misconduct. The practical challenge confronting both the regulators and the regulated is how to improve ethical decision-making without exacerbating the problem. Rule-makers must consider what kinds of substantive rules and rule formulations minimize the negative tendencies that inhere in rules, and the private sector needs to develop programs that will improve ethical climates.

Regulators

Regulations have traditionally addressed ethical matters implicitly, prescribing specific conduct without mentioning ethics. Prompted by the pervasiveness of corporate scandals, however, more recent regulations have begun to refer to ethics explicitly. Sarbanes-Oxley and the listing standards of the NASD and NYSE include provisions on codes of ethics, and the Federal Sentencing Guidelines now provide that maintaining a “compliance and ethical culture” may mitigate the sentence imposed on a corporate defendant.⁹⁷

⁹⁴ See Note, *The Good, the Bad, and Their Corporate Codes of Ethics: Enron, Sarbanes-Oxley, and the Problems With Legislating Good Behavior*, 116 HARV. L. REV. 2123, 2137-40 (2003) (hereinafter “*The Good, the Bad, and Their Corporate Codes of Ethics*”).

⁹⁵ See *id.*

⁹⁶ See Code of Ethics Release, *supra* note 30, § II.B2.c.

⁹⁷ See U.S. SENTENCING GUIDELINES MANUAL § 8B2.1(a)(2) (2005), available at <http://www.ussc.gov/2005guid/g12005.pdf>.

Yet whether ethics is the unstated basis of the prescription or is expressly mentioned, the relationship between the rule and ethics in these situations is *direct*. Rather than requiring ethical conduct or prohibiting unethical conduct generally, the rules prescribe specific conduct deemed consistent with accepted ethical norms.⁹⁸ Thus, a rule that prohibits murder or perjury focuses on particular behavior viewed as unethical. Similarly, typical corporate codes of ethics require compliance with specific regulations and internal policies.

This *direct* approach is useful as far as it goes, but it is limited by the inability to anticipate all situations that will require an ethical response, and by the undesirability of “legislating morality.” The direct approach, despite its prevalence, is not the only approach, however. Regulations can also deal with ethics *indirectly*. Such regulations would seek to foster conduct, not by requiring or prohibiting specific conduct directly, but by prescribing some other activity that, in turn, may reasonably be expected to engender the desired conduct. Good Samaritan laws illustrate the approach. Until the enactment of these statutes, well-meaning passers-by were often reluctant to aid their fellows (the ethical act) because doing so was not required and, if they did assist and did so negligently, they exposed themselves to a lawsuit.⁹⁹ The typical Good Samaritan law does not *require* that passers-by assist those in distress.¹⁰⁰ Instead, by raising the threshold beyond mere negligence for liability to attach, it creates a “safe harbor” for those who choose to aid someone in need. As a result, passers-by are *encouraged* to render assistance.

Several provisions of Sarbanes-Oxley apply this indirect approach. The section on whistleblowers, for example,¹⁰¹ does not require employees to blow the whistle, but removes some of the impediments to doing so. Similarly, the certifications required of the chief executive and chief financial officers¹⁰² are important not in themselves, but because having to certify will likely cause those executives to pay greater attention to the accuracy of their companies’ disclosure – which is the regulators’ real

⁹⁸ See Shavell, *supra* note 21, at 228 (“[L]aw and morality work together to control a vast range of behavior; notably, most crimes and torts are not only legally sanctionable but are also thought immoral, and often so are breaches of contracts and violations of regulation.”).

⁹⁹ See generally THANE ROSENBAUM, THE MYTH OF MORAL JUSTICE: WHY OUR LEGAL SYSTEM FAILS TO DO WHAT’S RIGHT 246-57 (2004).

¹⁰⁰ Several states in the United States have enacted duty-to-rescue statutes under which those who fail to aid someone in distress may be criminally liable. Generally, these have not been invoked or tested, but in many other countries, such a direct approach is an accepted part of the culture. See *id.* at 248.

¹⁰¹ Sarbanes-Oxley Act of 2002 § 806(a), 18 U.S.C. § 1514A (Supp. III 2003).

¹⁰² Sarbanes-Oxley Act of 2002 § 302, 15 U.S.C. § 7241 (Supp. III 2003); Sarbanes-Oxley Act of 2002 § 906, 18 U.S.C. § 1350 (Supp. III 2003).

concern. It may even be argued that the code-of-ethics provision is indirect: lawmakers did not enact it to give companies one more thing to disclose but, rather, to pressure companies to adopt and enforce codes in light of expected adverse publicity for companies without a code (or with one that was frequently waived).¹⁰³

Such indirect regulations have benefits not to be ignored. First, they may affect conduct beyond the narrow concern that prompted the rule. Thus, although certifications may enhance financial disclosures, they may also improve internal accountability generally, and they may strengthen the resolve of more junior employees – who may be asked to make “sub-certifications” on which the executive will rely – to insist on appropriate conduct. Second, even though indirect rules are subject to the same weaknesses as direct prescriptions – such as incompleteness and over- and under-inclusiveness – the consequences are often less severe. An executive may interpret the certification requirement technically and narrowly, or may use it as a “crutch,” for example, but it is difficult to see how his or her doing so will be any worse (and is likely to be better) than treating the disclosure rules themselves in such a legalistic fashion.

This is not the place for an extended discussion of various ways that indirect regulations might be used to improve ethical conduct, but one possibility – ethics training – deserves mention because of its close relationship to ethical decision-making. Since rule-makers can require some companies to have codes of ethics (and can require publicly owned companies to disclose whether they have such codes), regulators can also require that training be provided (or that companies disclose whether they provide such training). Since the Federal Sentencing Guidelines can make a “compliance and ethics culture” a factor in meting out sentences, they can also define that culture as one where, among other things, employees are trained to make ethical decisions.

Current continuing education and recertification requirements illustrate the potential. The securities industry continuing education program – applicable to both broker-dealers and their registered employees – is particularly relevant. The program includes a Regulatory Element, under which registered representatives must periodically complete a computer-based training session, and a Firm Element, under which every broker-dealer must assess its training needs annually, and develop and deliver an appropriate

¹⁰³ See *The Good, the Bad, and Their Corporate Codes of Conduct*, *supra* note 94, at 2132.

training curriculum. This program was approved in 1995 by the SEC, which recognized that training on compliance and ethical issues is closely linked to investor confidence:

[A] continuing education requirement for persons in the securities industry, administered pursuant to industry developed standards, will benefit public investors as a result of the increased knowledge and enhanced understanding of regulatory and ethical standards by industry members. SRO qualification of registered persons of broker-dealers is of critical importance in promoting compliance with the requirements of the federal securities laws. Increasing the sensitivity of registered persons to regulatory and ethical matters also should enhance investor confidence in the securities industry.¹⁰⁴

Significantly, the SEC has left it to the industry to develop content for the Regulatory Element, and the industry self-regulatory organizations have left it to the individual firms to develop content for the Firm Element.

While the Regulatory Element has recently been enhanced to include a module on ethics,¹⁰⁵ the Firm Element provides a model for rule-making designed to encourage ethical behavior in other industries. Regulators might require, for example, that such training include a component on decision-making (as distinct from specific prescriptions), and that, whatever else it covers, the decision-making component address organizational influences that challenge even the best-intentioned employees. Individual companies would then develop and deliver content relevant to their particular business, structure, and employees. Several suggestions for content follow immediately below.

The Private Sector

If ethics training is the *right* thing to do, then it should not matter whether it is the *required* thing to do. Business can take the initiative to develop a training program, and need not wait for regulators to require it. The larger issue is the scope of ethics training. Since the goal is to reduce the effects of rule limitations, a program that concentrates on regulations – what they permit and prohibit – will do little to move beyond those very weaknesses. This is not a reason to dispense with training about substantive rule requirements, but it is to urge that ethics programs focus more on values and provide employees with skills and support with which to decide ethical issues more effectively. It is the difference, for example, between listing various possible conflicts of interest, and training employees on how to recognize and avoid conflicts themselves:

¹⁰⁴ SEC Release No. 34-35341 at 9 (Feb. 8, 1995), <http://www.sec.gov/rules/final/nadce.txt>.

¹⁰⁵ See Securities Industry/Regulatory Council on Continuing Education, *Firm Element Advisory* 9 (2005), available at <http://www.securitiescep.com/FirmElements/posting/00002341.pdf>.

Enhancing individual abilities to recognize ethical issues and moral situations will increase the frequency with which employees make moral considerations, employ moral reasoning, and exercise moral theories, which will in turn facilitate the emergence of intentions to do good. . . . [W]e are not trying to impose a set of individual values on all employees. . . . Rather we are emphasizing improved moral sensitivity, improved moral decision making, and the encouragement of virtues like integrity and courage as they apply in a business setting.¹⁰⁶

A comprehensive discussion about the possible content of, and pedagogical approaches to, training on ethical decision-making is beyond the scope of this article. The purpose of the several brief comments below – organized according to the four-step model reviewed earlier – is to stimulate cross-disciplinary thinking about ways to apply our expanded knowledge of decision-making generally and of organizational influences in the context of ethics training.

Ethical Recognition

Employees sometimes fail to appreciate that their action or inaction really does affect other people. The eventual automobile driver may seem remote to the assembly-line riveter, the pensioner may not be top of mind to the mid-level accountant, the third-world baby may seem distant to the food processor, and the minor beneficiary's college education may seem years off to the back-office clerk. The human impact of conduct needs to be made more salient for the employees. Ethics training should encourage employees – through stories and testimonials of actual events (among other methods) – to consider the range of people (*e.g.*, customers, colleagues, shareholders, and members of the immediate or larger community) who may be affected by corporate misconduct.

Ethical Judgment

A universally accepted formula by which to decide an ethical question has thus far eluded mankind, so attempting to identify it in corporate training sessions will not be productive. Moreover, employees are quickly frustrated by a discussion of abstract principles, as any trainer who has heard employees plead “Just tell us what we can and cannot do” will attest. Instead, employees need to be stimulated to think beyond the confines of rules.¹⁰⁷ One way to do this is to pose dilemmas whose resolution does not involve readily ascertainable rules, including dilemmas where the choice is not between right and wrong conduct, but between several alternatives that may each be acceptable – but one of which

¹⁰⁶ Reynolds & Bowie, *supra* note 13, at 287.

¹⁰⁷ *Id.* See also RONALD R. SIMS, ETHICS AND ORGANIZATIONAL DECISION MAKING: A CALL FOR RENEWAL 148-49 (1994).

may be more right (or ethical) than the others.¹⁰⁸ A balance needs to be struck, however: if resolution of the dilemma is obvious, then little benefit is gained from training; if the ethical conduct is too subtle, then a clear teaching point may not be possible, and employees may not receive much direction from the training. A second possibility is to expose employees to experiments in human nature such as our tendency to engage in misconduct when ordered to do so by someone in authority,¹⁰⁹ and our tendency to make biased judgments (*e.g.*, risking more to avoid a loss than to make a profit,¹¹⁰ and irrationally giving undue weight to the short-term and to recent or otherwise salient situations¹¹¹).

The key is to infuse the training with situations that are realistic based on the employees' experience. Employees need to consider how notions of integrity, honesty, fairness, and similar values apply to such situations. They will benefit from participating in group discussions in which they are able to hear and react to how their colleagues think about the situation. By expanding employees' minds, this type of training should have a positive impact on decision-making skills.¹¹²

Resolving to Do the Ethical Thing, and Doing It

Ethics training cannot be limited to helping employees decide on the ethics of a situation, but, rather, must help employees to cope with those corporate dynamics that make doing the right thing difficult. These include peer pressure, the desire not to jeopardize job security, and our tendency to rationalize our behavior (*e.g.*, to believe either that we must be missing a crucial piece of information since our boss would never ask us to do something inappropriate, or that we can safely make an exception "just this once"). Again, describing or showing films of (or even replicating) actual experiments – including the well-known one in which Solomon Asch demonstrated the extent to which people will give clearly wrong answers due to peer pressure and the desire to conform¹¹³ – would seem to have considerable potential as a training tool. Training might also help employees recognize – and therefore be sensitive to the potential dangers – that it is sometimes just *more efficient* to follow a specific rule rather than to use limited mental

¹⁰⁸ See JOSEPH L. BADARACCO, JR., *DEFINING MOMENTS: WHEN MANAGERS MUST DECIDE BETWEEN RIGHT AND RIGHT* 6-7 (1997).

¹⁰⁹ See generally MILGRAM, *supra* note 46.

¹¹⁰ See generally Sunstein, *Hazardous Heuristics*, *supra* note 65.

¹¹¹ See, *e.g.*, Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, in *JUDGMENT AND DECISION MAKING: AN INTERDISCIPLINARY READER* 38, 46-49 (Hal R. Arkes & Kenneth R. Hammond eds., 1986).

¹¹² See Reynolds & Bowie, *supra* note 13, at 287.

¹¹³ See Solomon E. Asch, *Opinions and Social Pressure*, 193 *SCI. AM.* 31 (1955).

energy and time grappling with ambiguous principles, and to provide information about resources and strategies for dealing with this reality.

CONCLUSION

Discussions of rules and ethics usually deal with issues of *substance*, including the scope and legitimacy of rules, why rules should be obeyed, and the reasons why particular principles should (or should not) be used to resolve ethical dilemmas. The *nature* of rules and the psychological, physiological, and other aspects of the ethical decision-making *process* have been addressed much less frequently – and the consideration of a possible relationship between the nature of rules and the decision-making process has been rarer still. Yet the issue has been with us at least since the time of Confucius:

The Master said, “If the people be led by laws, and uniformity sought to be given them by punishments, they will try to avoid the punishment, but have no sense of shame.

“If they be led by virtue, and uniformity sought to be given them by the rules of propriety, they will have the sense of shame, and moreover will become good.”¹¹⁴

Rules are all-pervasive in society, but their inherent incompleteness becomes evident when their characteristics are examined. The over- and under-inclusiveness that is part of a rule’s essence renders rules incapable of applying to all situations, and prompts a need for some other sources of guidance – including ethics – to help us decide how to act. Ironically, however, the same characteristics that create this need also undermine our ability to utilize the guidance. Ethical recognition is harder because rules, by nature, discourage us from making choices; moral reasoning is impeded because rules fail to stimulate us to higher, post-conventional cognitive levels; moral resoluteness is weakened as external rules become – and are seen as – a greater motivator of conduct than our intrinsic values; and acting ethically is rendered more difficult because following rules is often simply less complex than considering and applying ethical principles.

In light of the counter-productive tendencies of rules, we must be cautious about the rules that we promulgate, and must minimize the inherent tension between rules and ethical decision-making. Our goal must be to use our considerable (and ever-expanding) theoretical and practical knowledge creatively to

¹¹⁴ CONFUCIUS, CONFUCIAN ANALECTS, THE GREAT LEARNING AND THE DOCTRINE OF MAN 146 (James Legge trans., Dover Publications 1971) (1893).

improve the skills and confidence with which employees and others address their ethical dilemmas, empowering them to move beyond the confines of “legal” to the realm of “ethical.”