



# The New World of BUSINESS ETHICS

BY PHIL HOLBERTON

*If you are not in the finance department or don't work closely with the corporate legal department, you will probably be less involved than those in senior management. Still, there are central aspects of the Sarbanes-Oxley legislation that you should be aware of.*

ILLUSTRATION: DEREK BRIGHAM

## CODE OF ETHICS

The Securities and Exchange Commission (SEC) mandates that, effective with annual reports for fiscal years ending on or after July 15, 2003, public companies must disclose whether the company has a code of ethics for its senior financial officers. What company will want to check off no to this question?

Also, both the Nasdaq and the New York Stock Exchange have proposed requiring that, in order to be listed, companies must have adopted codes of ethics covering all employees. Inescapably, all affected companies will develop such a code and, in some fashion, distribute it to all their employees. Megan N. Gates, an attorney at the law firm Mintz Levin Cohn Ferris Glovsky & Popeo who specializes in the area of corporate governance and topics related to the Sarbanes-Oxley Act, says, "I expect all companies will distribute codes to their employees for review and understanding. What I can't predict at the moment is how many of the companies will require their employees to acknowledge receipt and compliance."

Back in the 1970s, the passage of The Foreign Corrupt Practices Act resulted in a wild flurry of corporate ethical guiding principles being distributed to employees as corporate America moved to react to that legislation. Today, with the advent of the Internet, many companies are specifically posting their ethics codes on their Websites. Take for example Aon Corporation, based in Chicago, Illinois. Every employee received a letter from the company's CEO, Patrick Ryan, and was made aware of the importance of ethics to the company. In addition, AON has published on its Website the company's 21-page "Business Conduct Guidelines" for the entire world to view. If you work for an organization that has yet to establish a written code of ethics, there are role model organizations available, like AON, to learn from. Many of the larger companies have tackled this issue head on and have developed these codes already.

## EMPLOYEE WHISTLEBLOWING

Although whistleblowing is not specifically defined in the Act, it generally can be characterized to mean reporting questionable matters to higher levels of management within the organization or to federal or state legal authorities. The Sarbanes-Oxley Act specifies that the audit committee of the board of directors has the ultimate responsibility for establishing detailed procedures regarding treatment of confidential and anonymous complaints about questionable accounting and auditing matters. But since I generally believe all public companies will be establishing a comprehensive code of ethics for all employees, most companies will probably charge their human resources department with creation of a more comprehensive set of procedures—procedures also designed to provide anonymity for the reporting of violations of the company's code of ethics. In the end, the audit committee will need to sign off on the procedures and be comfortable that they are workable in practice.

Under Sarbanes-Oxley, there cannot be any retaliation against employees if they "blow the whistle" because they believe there has been a violation of rules or regulations of the SEC or of other federal laws. The Act calls for criminal penalties that can be levied against the retaliator—ranging from a fine to a prison term. It's hard to say, yet, how all this will play out in practice. It is not in anyone's interest to have retribution and those companies that fully embrace the spirit of the legislation will want to be sure that complaints (and not just those relating to accounting and auditing) are taken seriously.



Here's an example of one company's approach. Any AON employee who believes there is unethical behavior taking place in the company can call a hotline that is monitored by senior members of the human resources function. The company's guidelines deal right up front with the issue of retaliation, indicating, "retaliation against anyone for exercising their rights under this policy will not be tolerated."

The establishment of whistleblowing procedures by the audit committees of public companies is not required to be fully implemented until 2004; therefore, many companies currently are in the process of establishing mechanisms for reporting whistleblowing actions. However, the criminal provisions of the Act prohibiting retaliation against whistleblowers took effect immediately upon passage of the Act, on July 30, 2002.

## **ENHANCED FINANCIAL DISCLOSURE**

Another part of the new legislation deals with proper reporting to shareholders through enhanced financial disclosure. Although this part of the legislation does not affect most employees at large, it does have an effect on those individuals in the financial departments.

## **TWO IMPORTANT AREAS FOR IMPROVED DISCLOSURE**

Each public company is required to review and assess internal controls annually in a report that states the responsibility of management for establishing and maintaining the company's internal control system. The report should contain an assessment of the system's effectiveness as of the end of the company's most recent fiscal year. In all organizations, but especially in complex organizations with many different accounting systems and operating units, a methodology needs to be established for collecting the information for assessment.

The Sarbanes-Oxley Act also mandates that companies provide full and fair disclosure of material information to their shareholders.

## **IN CONCLUSION**

Most public companies are working fervently to comply with the legislation. Of course, it is impossible to legislate ethics, as ethics stem more from an individual's core values. On the other hand, a company's senior leadership team has a responsibility to comply with the law. If corporate executives combine the spirit of the legislation with the actual technical requirements, we should see a sharp falloff in corporate catastrophes. What are the roles of managers and employees in all this? They should become familiar with their company's code of ethics and have the courage to raise questions and report violations without fear of recriminations.

Although these requirements apply to public companies, leaders of privately held companies, both large and small, should take a lesson from this legislation and adopt similar codes of ethics and compliance procedures.

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