IMPLEMENTING AND AUDITING ETHICS PROGRAMS

The Ethics audit

*Ethics audit* is a systematic evaluation of an organization’s ethics program and performance to determine whether it is effective.

The audit provides an opportunity to measure conformity to the firm’s desired ethical standards.

A *social audit* is the process of assessing and reporting a business’s performance in fulfilling the economic, legal, ethical, and philanthropic responsibilities expected of it by its stakeholders.

Ethics auditing is similar to financial auditing in that it employs similar procedures and processes to create a system of integrity that includes objective reporting.

**Differences between ethics auditing and financial auditing**

Whereas financial auditing focuses on all systems related to money flow and on financial assessments of value for tax purposes and managerial accountability, ethics auditing deals with the internal and broad external impact of the organization’s ethical performance.

Ethics auditing is not usually associated with regulatory requirements, whereas financial audits are required of public companies that issue securities.

**Benefits of ethics auditing**

1. Recent accounting scandals and legal and ethical transgressions have encouraged companies to better account for their actions in a wide range of areas, including corporate governance, ethics programs, customer relationships, employee relations, environmental policies, and community involvement.
2. The assessment of the ethical culture of an organization is necessary to improve ethical performance and to document in legal proceedings that a firm has an effective ethics program.
3. The auditing process can highlight trends, improve organizational learning, and facilitate communication and working relationships.
4. Improved relationships with stakeholders who desire greater transparency.
5. Regular audits permit shareholders and investors to judge whether a firm is achieving the goals that it has established and whether it abides by the values that it has specified as important.

**Ethical Crisis Management and Recovery**
An ethics audit can discover rogue employees who are violating the firm’s ethical standards and policies or laws and regulations.

Ethical disasters follow recognizable phases of escalation, from ethical issue recognition and the decision to act unethically to the organization’s discovery of and response to the act.

The global financial crisis has only heightened the need for organizations to implement due diligence ethics and compliance programs to restore confidence and competitiveness. The ethics audit becomes a key part of this review and management process.

**Risks and Requirements in Ethics Auditing**

Although ethics audits provide many benefits for individual companies and their stakeholders, they do have the potential to create risks. For example, a firm may uncover a serious ethical problem that it would prefer not to disclose until it can remedy the situation.

Moreover, the auditing process imposes burdens (especially with regard to record keeping) and costs for firms that undertake it.

Many companies that engage in suspected misconduct find that public scrutiny of their practices causes them to conduct an ethics audit to show concern and respond appropriately to weaknesses in their ethics program.

Although ethics and social responsibility are defined and perceived differently by various stakeholders, a core of minimum standards for ethical performance is evolving.

**The Auditing Process**

1. **Secure Commitment of Top Managers and Board of Directors**
   The first step in conducting any audit is securing the commitment of the firm’s top management and, if it is a public corporation, its board of directors.
   Pressure for an audit can also come from top managers who are looking for ways to track and improve ethical performance and perhaps give their firm an advantage over competitors that are facing questions about their ethical conduct.

2. **Establish a Committee to Oversee the Ethics Audit**
   Ideally, the board of directors’ financial audit committee would oversee the ethics audit, but this is not the case in most companies. In most firms, managers or ethics officers, who do not always report to the board of directors, conduct social and ethics auditing.
   This team should include members who are knowledgeable about the nature and role of ethics audits and come from various departments within the firm.

3. **Define the Scope of the Audit Process**
   The ethics audit committee should establish the scope of the audit and monitor its progress to ensure that it stays on track.
   This scope depends on the type of business, the risks faced by the firm, and the opportunities available to manage ethics.
Assessments can be made on the basis of direct consultation, observation, surveys, or focus groups.

4. **Review Organizational Mission, Values, Goals, and Policies and Define Ethical Priorities**
   Because ethics audits generally involve comparing an organization’s ethical performance to its goals, values, and policies, the audit process should include a review of the current mission statement and strategic objectives.
   This review step should examine all formal documents that make explicit commitments to ethical, legal, or social responsibility, as well as less formal documents, including marketing materials, workplace policies, and ethics policies and standards for suppliers or vendors.

   It is also important to examine all of the firm’s policies and practices with respect to the specific areas covered by the audit.
   At some point, the firm must demonstrate action-oriented responsiveness to those ethics issues it has given top priority.

5. **Collect and Analyze Relevant Information**
   Identify the tools or methods for measuring the firm’s progress in improving employees’ ethical decisions and conduct.
   The firm should collect relevant information for each designated subject matter area.
   Some techniques for collecting evidence might involve examining both internal and external documents, observing the data-collection process (such as by consulting with stakeholders), and confirming information in the organization’s accounting records.
   Because integrating stakeholder feedback in the ethics audit process is so crucial, these stakeholders must first be defined and then interviewed during the data-collection stage.

6. **Verify the Results**
   Have an independent party—such as a social/ethics audit consultant, a financial accounting firm that offers social auditing services, or a nonprofit special interest group with auditing experience—verify the results of the data analysis.
   Although the independent validation of ethics audits is not required, an increasing number of companies are choosing to do so, much as they have their financial reports certified by a reputable auditing firm.
   The process of verifying the results of an audit should involve standard procedures that control the reliability and validity of the information.

7. **Report the Findings**
   This involves reporting the audit findings through a formal report to the relevant internal parties—namely, the board of directors and top executives—and, if approved, to external stakeholders.

**The strategic importance of ethics auditing**

The ethics audit, like the financial audit, should be conducted regularly rather than in response to problems involving or questions about a firm’s priorities and conduct.
The ethics audit provides an assessment of a company’s overall ethical performance as compared to its core values, ethics policy, internal operating practices, management systems, and, most important, key stakeholders’ expectations.

Most managers view profitability and ethics and social responsibility as a trade-off. This “either/or” mindset prevents them from taking a more proactive “both/and” approach.