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## **Integrating Sarbanes-Oxley, Leadership and Ethics**

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As reported in various sources in the recent past, corporate scandals have dramatically eroded the public trust and confidence in corporate reporting. Such a lack of confidence has been a contributing factor to the recent slowdown in the U.S. capital markets. As a result, Congress aggressively responded by enacting the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley). This major legislation has created a new system of checks and balances that will have a significant and long lasting impact not only on corporate America, but also the independent public accountant.

In reading the Act, many new rules and guidelines have been and continue to be developed by various bodies, especially the U.S. Securities and Exchange Commission (SEC) and the Public Company Accounting Oversight Board (PCAOB). However, compliance with Sarbanes-Oxley will not by itself ensure that corporate scandals will not reoccur. Just as morality cannot be legislated, behavior and actions that lead to unethical actions cannot be legislated.

Investor trust is premised on a strong and viable corporate system. At the foundation of such a system is a code of ethical behavior that focuses on the best long-term interests of the corporation which results in the best long-term interests of the corporation's stakeholders. However, in a recent survey of individuals who could be trusted, CEOs of large corporations fared very poorly. Of those surveyed, 73% responded that CEOs could not be trusted! (CNN/USA Today/Gallup Poll, July, 2002).

An important challenge to corporations and CEOs is the creation of a "tone at the top" that sets an example of a corporate culture that promotes ethical conduct that permeates throughout the corporation. Such an ethical environment supports responsible corporate behavior to address any misconduct beforehand, rather than waiting to react after the damage has been done. A major component of such an environment is the quality of corporate leadership.

As business leaders, we must make ethics our very top priority. In fact, it is no longer possible to do otherwise and survive. It's time for a new business model to emerge from the ashes, one in which ethics and profitability walk hand-in-hand. In fact, this ethical issue is so important that Sarbanes-Oxley now requires public registrants to have corporate codes of ethics!

Developing a comprehensive solution to mitigate an organization's exposure to unethical activity is very difficult; you are fighting the legacy that got you where you are now. You and your colleagues are products of several decades

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of business school theory that says money always comes before humanity. Old habits die hard.

The **very foundations** of the business establishment were shaken by the specters of insider trading, manipulative accounting, and out-and-out fraud. The solution must impact the very foundations of the business establishment, and the outcome must be profound, sustainable and self-improving.

A comprehensive solution should address what is undoubtedly more than one fundamental issue or cause. We must avoid the temptation to implement a quick-fix, one that addresses a subset of the root-causes and naively assumes that process and punishment will keep us safe from harm.

Sarbanes-Oxley, the compliance requirements and punishment for non-compliance is a critical part of the solution. The remainder of the solution consists of components that address:

- Sustainability
- The Role of Leadership
- Behaviors and Attitudes throughout the organization
- Continuous Improvement

The final consideration is a tool to enable the solution. The Leadership Diamond® philosophy and approach has proven itself over 35+ years as the mechanism enabling foundational change in corporate and personal actions.

## **Introduction**

Sarbanes-Oxley is clearly an important and unfortunately necessary legislative action to change financial practice and regulate corporate governance. However, compliance will not by itself ensure that the high profile corporate scandals involving such companies as Adelphia, Enron, and Worldcom will not manifest themselves again.

It is not enough to perform business process innovation to reengineer corporate processes. It is not enough to perform audits of an entity's internal control and financial statements in hopes of ensuring that the organization is following the reengineered processes. Compliance with Sarbanes-Oxley does not remove the catalysts that brought about the unethical behaviors and actions that caused the scandals.

The Board of Directors will still demand results that meet or exceed past performance. The Stock Analysts will continue to focus on bottom line results. The shareholders will continue to demand return for their ownership of the company. In fact, one could argue there is now more pressure on executives to drive outstanding corporate results. There is certainly more scrutiny from the press and the SEC. Customers, investors, the government,

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activist groups and the media are all more aware and involved in watching corporate results than before.

The **very foundations** of the business establishment were shaken by the specters of insider trading, manipulative accounting, and out-and-out fraud—highly publicized scandals that have sent consumer confidence spiraling almost as fast as the stock market.

The solution must also shake the very foundation of the business establishment. The outcome from implementing the solution must be profound, sustainable and self-improving.

Crucial to determining the components of a sustainable solution is determining the fundamental cause(s) of the scandals. The fact that the perpetrators did not follow established processes, or that the established process and procedures were weak, is not the fundamental issue.

Regardless of how much pressure the perpetrators experienced from their leadership, the Board of Directors and the marketplace, regardless of what processes the perpetrators chose to follow, the fundamental issue is that the perpetrators, of their own freewill, chose to participate in unethical behaviors and actions.

Just as morality cannot be legislated, ethical behavior and actions cannot be legislated.

### **Ethics as the New Corporate Asset**

Ethics must become a business principle that exists in practice. Each company must develop a mechanism for successfully communicating and integrating such values into their cultures. Ethics is positioned to become the new corporate asset, as investors and customers are distinguishing between companies that have truly embraced an ethics-based approach to business and those that have not.

A profound paradigm shift is occurring, one that takes the spotlight off the hard dollars & cents skills we've always been taught, and shines it on ethical considerations.

As business leaders, we must make ethics our very top priority. In fact, it is no longer possible to do otherwise and survive. It's time for a new business model to emerge from the ashes, one in which ethics and profitability walk hand-in-hand.

In the post 9/11 era and amidst the current business ethics crisis, it is no longer possible to fake credibility. Trust is now a function of a person's and

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an organization's true ethics. To be believable is no longer advertising and public relations. People nowadays demand substance.

The sooner executives get this message, and the more promptly they understand that this in fact has always been a human axiom, the quicker will confidence in the capital markets and our economic prosperity return.

Today's executives are required to be whole persons and create companies that are whole. Excesses in one area -- such as ruthless reliance on the facts and the numbers exclusively -- and neglect in another -- such as ignorantly minimizing the emotional catastrophes that accompany downsizing and M & A's -- predict an enterprise's Wall Street ruin.

Being razor sharp strategically -- as was Enron, but lacking the common courage to put wild risks into cool perspective -- cascaded a company from the crowning jewel of opulence to the dark abyss of bankruptcy. Refusing to be whole is the recipe for meltdown.

Likewise, at Arthur Andersen, Barbara Toffler, author of *Final Accounting* and former partner of Andersen's Ethics & Responsible Business Practices consulting services, traced the roots of Andersen's ethical missteps and revealed the gradual decline of a major accounting firm and its once-proud culture. She reported that ambition, greed and a lack of internal ethics was the downfall of Andersen.

Incomplete human beings, skewed in their personal development, become defective managers. To survive in today's ethics breakdown requires executives who mobilize their full human potential.

How does one do this? How can you increase real profits with true ethics? The first step is to begin the journey to embrace Ethics through effective and appropriate Leadership actions and behaviors.

### **Understand the Challenge**

Don't fool yourself: change of this magnitude is seldom easy. It's better to realize this truth up front. Here are just a few of the truths that will make aligning yourself with the new paradigm challenging, indeed:

You're fighting the legacy that got you where you are now. You and your colleagues are products of several decades of business school theory that says money always comes before humanity. Old habits die hard. It will be a struggle to change and it won't happen overnight.

People inherently resist change. This is not news. You can expect resistance from every quarter, including periods of "second-guessing" yourself.

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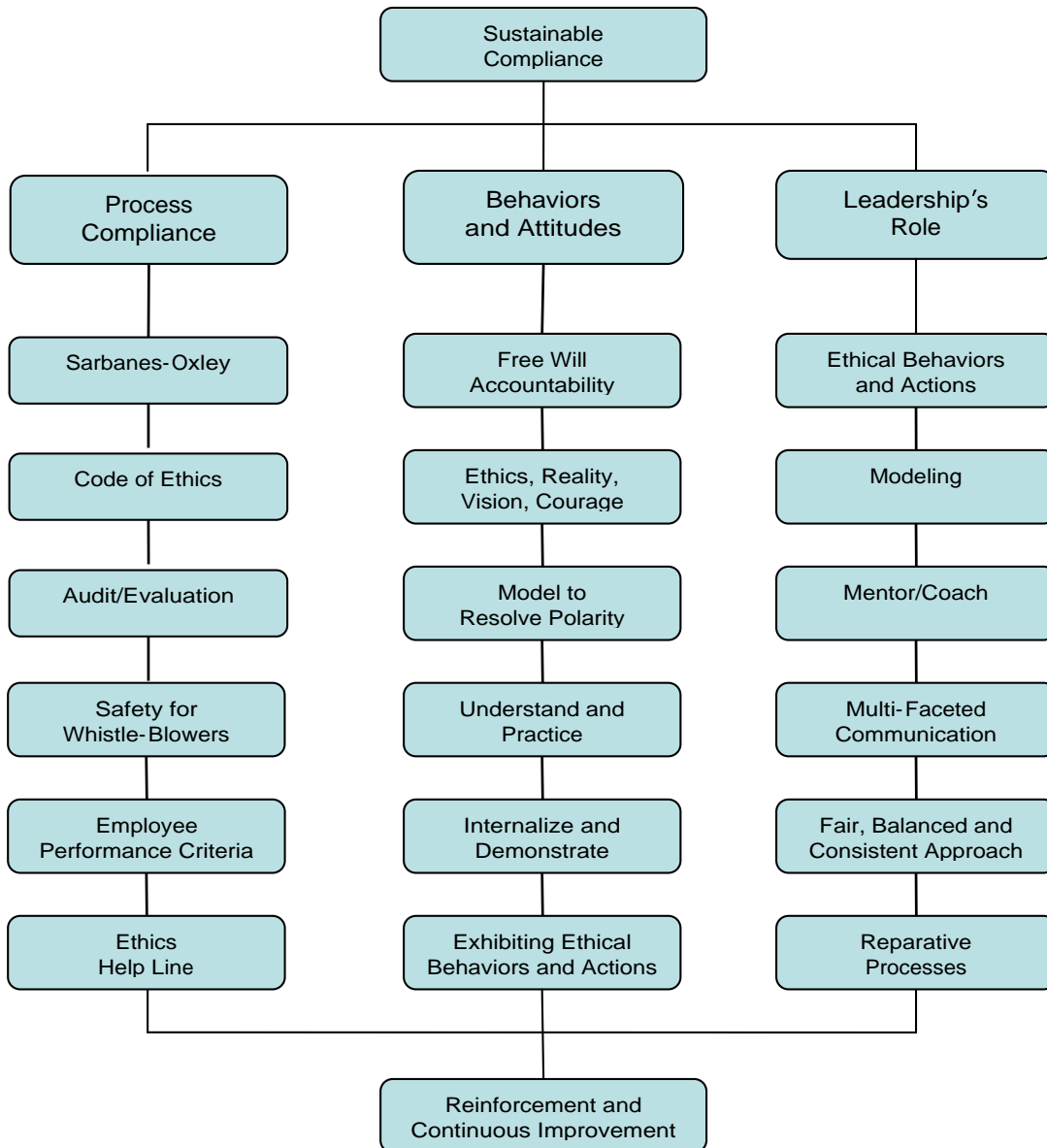
You're trying to make a major change in a bad economy. There's more pressure than ever to be profitable, not in order to beat last year's figures but in order to survive. This will make going in a whole new, unfamiliar direction very frightening.

None of this is meant to be discouraging. In fact, it's intended to help you better prepare yourself for the exciting process that's about to unfold.

### **The Comprehensive Solution**

The solution consists of a multi-faceted approach, developing and deploying a strategy that incorporates:

- Process compliance and price of non-conformance (Sarbanes-Oxley)
- Behaviors and attitudes throughout the organization
- The role of leadership
- The tool to enable sustainability: Leadership Diamond® Realisms



## The Process

The Process is answered by Sarbanes-Oxley. The remainder of the solution is in place to assist the organization in internalizing Ethical behavior. Without that internalization, Sarbanes-Oxley becomes a nuisance to those unethical minds that must now be challenged to find a way around this latest intrusion.

## Leadership Diamond® Realisms

There are four Leadership Diamond® realisms that are fundamental to any leader: *Freedom, Principle, Realism, Grand Strategy and Accountability!*

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## ***Freedom Is the Foundation***

The foundation of all successful leadership is the full-bodied understanding and application of the fact that as human beings we are free. We are born with free will, we have free will, we can never relinquish our free will. Until our dying day will we have free will. Free will is a clear experience. Free will makes ethics possible. Free will is the source of our power and the origin of our anxiety. It is overwhelmingly our deepest truth as persons, as human beings.

And the most profound act our Country asks of us is that we be prepared to give our sacred lives for the preservation of our Nation's freedom! Usual leadership theory tell us how to influence people's thoughts and people's feelings. And leadership coaching is to help leaders convince personnel to *think* and to *feel* in ways helpful to a business' bottom line: *think* of the mission of the company and *feel* loyal and joyful towards the company. What is missing, however, and grossly so, in fact, critically, is the *will*. We believe that workers think and feel, have ideas and emotions. But that is not enough.

We have in modern times ignored the much more fundamental reality of a third phenomenon in the soul, in addition to thoughts and feelings, and that is the *will*, the *will* that is *free*. And without a clear understanding of free will, and the expertise to talk lucidly about free will to the people for whom you are responsible, leadership is a desiccated recipe.

Leadership is to know, learn, and teach the ascending ladder of freedom, free will, consequences, responsibility, ownership, accountability, and ultimately choosing accountability for the sake of both financial necessity and existential honor.

Here, in the inner zone of freedom and free will, lies the bedrock of your health -- of your body, of your loves, and of your pocketbook. As leader, you are a secular apostle preaching the power of freedom. This is the true and final meaning of ethics in business.

## ***Leaders Choose Principle***

Leaders freely choose to live by principle. The famous eighteenth century German ethicist Immanuel Kant wrote "Two things fill the mind with ever-increasing wonder and awe, the more often and the more intensely the mind of thought is drawn to them: the starry heavens above me and the moral law within me."

The moral law within me! Don't we all sense it, if we hold still and listen in the silence? We all have a conscience. It draws us like a magnet to principle. It is never selfish. Human beings surprisingly tend to agree about what it says.

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Conscience and the moral law have a mysterious draw on us, a strange claim. We can distinguish good from evil, right from wrong, ought from ought not. It is in some inexplicable way related importantly to respect, pride, dignity, and self-esteem.

We seem to understand that we have a duty, a destiny, a task in life -- even though there can be debate about its precise content. It is aroused by words such as "fairness," "justice," "equality," and "liberty." The *Declaration of Independence* and the *Constitution* resonate movingly to something inside that can only be called our conscience.

Unless we respond to that part of our inner, our psychic, our mental equipment -- as powerful as it is also enigmatic, as dramatic as it is also unavoidable -- we skirt the perilous edge that we in fact have thrown away our very life. What horror! Authentic leaders turn back from greed and selfishness, from narcissism and naïve values, to return instead to a serious investigation of the things that matter most, of what is enduring, of what is genuinely worthy, of what is honest, of what is generous, and what feels clean.

True value is not what one person or one sect dictates to the rest of us. True value results from honest and collective examination of who we are, where we come from, and where we are going. The poet Rilke said, "Do not seek answers; live the questions." After 9/11 and the business ethics crises, leaders can no longer avoid this stentorian call to authenticity.

### ***Realism Is a Way of Life***

Most pervasive in the late nineties has been the ruthlessness of realism, hardly requiring analysis and description. In the US' extreme capitalism we had vastly overdone it. Europe's more socialistic outlook had tried to tone it down. Europe's economies are failing because realism has not been sufficiently emphasized. And the US economy is failing because there realism has been excessively overemphasized. What Aristotle called the Golden Mean has been missing on both sides of the Atlantic.

Being fully in touch with the real world is the psychological and psychiatric definition of mental health. And yet no person can stand the anxiety of being one hundred percent aware of what is real. It can be as searing as staring directly into the sun.

Realism is more than the numbers: it means you never lie to yourself, you do not deny the truth about yourself. You know that when something hurts, when you get inordinately angry, upset, i.e., enraged, when you turn irrational, it is because you are threatened fundamentally, for you secretly agree with the insult and the indictment. You can no longer let it go and, in fact, as a last resort, you expel this shadow insight about yourself, forcibly

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and in despair, from the presence of your consciousness. Each person has a site of inferiority. There, when that point is touched, you are sensitive, and there, when reminded, you become virulently defensive.

There you say, not that you *think* you are inferior, but there in your depraved image of yourself you say that in fact you *are* inferior! But you keep the secret and get furious at anyone who so much as dares to point it out to you.

Coming to terms with that dark reality, accepting that perception of yourself, is conversely, indeed, the very heart of your strength and your power as a rightful leader of men and women.

Once reconciled with your shadow, you can take criticism, fair or unfair, you can tolerate put downs, deserved or not, you can endure defeat, expected or not, and you can survive disgrace and humiliation.

To get there is realism beyond the statistics and strikes right at the core of your emotional intelligence. People with power are both adulated and hated above what is appropriate and beyond of what is reasonable. They can stomach it, even thrive on it and learn from it, and teach others how under such circumstances not only to preserve their dignity but actually to magnify it.

For to restore your inner self-respect when logic is against it, is to “pull yourself up by your bootstraps.” That is why life confronts us with its tests and furnishes us with their messages.

This is that corner of the soul which receives well its baptism of fire.  
Have you passed the test?

### ***Grand Strategy Is a Rare Virtue***

Little is more clearly the mark of an authentic leader than the commitment to Grand Strategy.

We use an exercise that unfailingly enlarges the scope of the executive mind. Take any big news story, the kind that mesmerizes the population -- the War on Terror, Weapons of Mass Destruction, the once envied and lionized CEOs now facing censure and threatened with jail sentences, the Gulf War, an airplane crash, a major Olympic victory, an election upset, a sensational trial, the impeachment of a President, suicide bombers, and of course 9/11 – and ask the overwhelming question: *what deep lessons are there for you in how you conduct your business and your life? What messages, what learning, about the things that you control can you derive from an enlarged perspective of this or any other monumental and historic event?*

The Gulf War taught us the importance of high technology and the use of overwhelming force. The War on Terror teaches us that worldly inequalities

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lead to dangerous instabilities affecting everyone. Impeachment teaches us that dubious actions have unexpected and dramatic consequences, and sports victories teach us the power of persistence, commitment, focus, and dedication. You then ask yourself, in your depth, *how does that today apply to me and to my business?* To do this Grand Strategy exercise with inspiration and creative innovation is indeed an uncommon attribute.

### **Accountability**

Recognize that, whether you are an individual performer or C.E.O., you have the Freedom to choose whether you behave in an Ethical manner. Once you recognize that it is your choice to act in whatever manner you feel is best at that point in time, you have opened the door to embracing Accountability.

You are Accountable for your decisions and actions and the outcome of those decisions and actions. As a leader, you must first accept Accountability for your decisions and actions.

Once you have accepted Accountability for your own decisions and actions, as a leader your fundamental action becomes to not only to *talk* about accountability, not only to encourage people in being accountable, but first and foremost to take an *action* indeed: and that is to **hold** people accountable, not only through words but primarily in deeds.

*Holding* people accountable is an action, the result of a decision, the results of a courageous step -- grounded on initiative, free choice, and managing the ensuing anxiety of isolation. This means to avoid as non-negotiable what in accountability theory are called *irresponsibility enablers* and *irresponsibility co-dependencies*.

The actions are to choose personal consequences (i.e., withholding funds) and to choose not to interfere with natural consequences (i.e., business breakdown and bankruptcy).

As leader, you are expected to model accountability in your words and deeds, i.e., in your language and in your behavior.

### **The Role of Leadership**

The catalyst for the implementation of the solution lies with the Leadership of the organization. Those who do behave ethically will thrive, both financially and in other ways. *Every* conscientious businessperson should make it a priority to explore what ethical behavior is, and how he or she can make ethical decisions.

**Dr. Warren Bennis**, in Leader to Leader No. 23, Spring 1999: "Research at Harvard University indicates that 85 percent of a leader's performance depends on personal character."

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Dr. Bennis goes on to say: "Exemplary leaders create a climate of candor throughout their organizations. They remove the organizational barriers -- and the fear -- that cause people to keep bad news from the boss. They understand that those closest to customers usually have the solutions but can do little unless a climate of candor allows problems to be discussed.

Especially during times of change, exemplary leaders share information about what's going on in the organization, the industry, and the world. They treat candor as one measure of personal and organizational performance, which can be gauged through employees' response to such statements as, "My organization encourages people to take the time to communicate openly, even about difficult questions." Or, "There is little fear of speaking openly about important issues."

Without candor there can be no trust. And by building trust, leaders help create the reliability and consistency customers demand."

Character is the key to Leadership!

In other words, it's not just doing the right thing, but doing the right thing for the right reasons. A leader must change not just his or her business practices, but also his or her heart. When the leaders are walking the talk and fighting the good fight, then the organization observes and begins to follow.

The first step, then, to becoming whole lies in courageous decisions -- to be authentically *open-minded*, to make self-transcending *commitments*, and to be responsible to help co-create a *communal culture*. That is ethics in action!

### **Behaviors and Attitudes**

In a hotel in New York, everywhere is written "Attitude is Everything." It's words. No one feels it. This truth is neither understood nor executed. The true leader sees this yardstick as a human value, a form of love and service, and not as a PR gimmick. As the former, it works in business. As a latter, it is a fraud that alienates.

If a tree is dying, don't just prune it but examine the soil. If a building is tilting, don't just analyze the steel beams but check the foundations. If aspirin does not lower the fever, take X-rays and blood samples. And if a business is failing examine the leadership attitudes for lack of ethical excellence and ethical greatness.

Authentic leaders teach messages to their people which transform the company culture. Authentic leaders help awaken these attitudes in their people.

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All leadership attitudes are needed. All leadership attitudes are ethical values. One alone will not do. Attitudes precede techniques. A how-to guide without right attitudes are empty mechanical gestures. Computers do not lead people. If that should ever happen, civilization will be finished, humanity will have disappeared, and there no longer is anything left to lead!

"What many people don't understand is that a company can do *right* and still do *well*," he says. "The two are not mutually exclusive. In fact, doing right is an integral part of doing well. I don't have to tell you what happens when a company fails to do right; just turn on the news and you'll see plenty of examples. But that doesn't mean it's impossible to place *too much* emphasis on Ethics to the detriment of the other three facets of the Leadership Diamond."

### **Sustainability and Continuous Improvement**

The following general concepts represent not a detailed plan, but only a starting point for the effort. These prerequisites will assist in defining an environment where Sustainability in Ethical Behavior is the norm and Growth in the Internalization and Application become commonplace.

#### ***Treat Ethics as a "Northbound Train"***

A Northbound Train relates to a drop-dead have to support initiative. The staff either gets on the Northbound Train or they leave. Ethics is 100% or nothing.

Before your new policies and procedures are implemented company-wide, it's critical to get the entire executive team to do more than just buy into the vision, they have to walk the talk, practice it, say it, teach it and show it in their actions and words.

That way you will present a united front to the rank and file. When employees see you putting your money where your mouth is—actually demonstrating ethical behavior and making the hard decisions—they will be far more likely to do the same.

#### ***Decide What "Ethical" Means for your Company***

Sit down with your executive team and figure out where ethical lapses may exist. Include stockholders, employees and customers in your equation. Sometimes it's easy to make these determinations. Sometimes it may take a great deal of soul-searching to uncover them.

Be brutally honest, and keep digging, even if it's painful. Ultimately, you will emerge with an ethics statement that represents the kind of company you want to be.

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### ***Spell Out New Policies in Excruciating Detail***

The word “ethics” means different things to different people. Do not leave its meaning open for interpretation. Be specific when writing up your new policies & procedures document. This is where the rubber meets the road in transforming your company. Of course, it’s important to remember that these policies are not carved in stone—time and experience may reveal detrimental unintended consequences that come with your early decisions. In the future, it might be necessary to amend the document. That’s okay, as long as you don’t go against the spirit of the ethical vision with which you started.

### ***Invest in Training and Workshops Supporting Sustainability***

Unfortunately, implementing your new ethics-based policies and procedures is not as simple as sending out a memo that says, “Okay, we’re all going to be ethical now!” You have to not only tell employees specifically *what* is to change (your new policies and procedures), but also *how* to go about making these changes. It is here that proper training can make a world of difference.

“We strive to help our clients create unity between business and ethics,” Koestenbaum explains. “This creates a win/win situation for everyone. We present an image of what a human being is, based on thousands of years of the history of the humanities, and condense that history into a few impactful, high-intensity principles. And they really seem to work.”

### ***Conclusion***

Be Steadfast—never, never, give up. As we discussed earlier, change of this magnitude is not something that happens overnight. When the going gets rough—and it will—you may be tempted to revert to your old ways. Resist this temptation.

Remember, transforming your company to mesh with the new paradigm of ethics is much more important than some “flavor of the week” initiative that’s scrapped at the first roadblock you encounter. This is where the real work of change is accomplished—holding the line in the minutiae of everyday business.