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Lord Brian **Griffiths of Fforestfach**, House of Lords, Goldman Sachs International, London

Ethical Challenges in the Work Place

My contribution to this conference is simply to set out some ethical challenges which those of us on the front line in business face in today's competitive, global workplace.

For the first decade of my career at the LSE I viewed business from the perspective of an academic economist. In the standard theory of the firm, the assumption is made that firms maximize profits which subject to the degree of competition in market structures, produce different results for prices and output. In this approach ethical considerations are irrelevant. The next decade I spent at CASS Business School in order to better understand how business firms reached decisions in particular and the role played by culture and values. Following working in 10 Downing Street in 1991 I moved to Goldman Sachs as an international advisor and for the past decade or as a non-executive board member of Goldman Sachs International and Goldman Sachs International Bank.

During the whole of this period I have sat as a non-executive director on the boards of some fourteen companies. These have included firms quoted on the (New York Stock Exchange (NYSE), Nasdaq, London Stock Exchange (LSE), private equity firms and subsidiary operations of larger companies. The first board I sat on before I went into government was the Court of the Bank of England. The activities of these companies have ranged from office furniture to cleaning, television, music, care homes, railways, newspapers and banking.

I have never been a full-time employee or executive of any company but from my broad experience as a non-executive and adviser I would like to highlight a number of ethical issues with which I, and others in business, have had to grapple.

The Purpose of Business

One challenge has been to answer the question, what is the purpose of the business for which I work? One response, especially by economists, is that the overriding purpose of a business must be to maximise profit or shareholder value by increasing revenue, controlling costs, gaining market share and producing a greater return on equity. This view should not be dismissed out of hand because it has a number of strengths. It is a simple rule, with a single objective, which is easily measured. It allows business freedom in making decisions. It focuses on performance and profit, which are vital if a company is to continue to raise capital and remain in business.

However, it suffers from a number of weaknesses. A business is a community of people not just a bundle of contracts. People have an innate sense of what is right and wrong, just and unjust, rewarding and unrewarding in business as in other areas of life. Adam Smith observed that the wise and judicious person would display the virtues of prudence, justice and beneficence in all walks of life including commerce, resulting in restraint, industry, fragility, sobriety, honesty, civility and reliability. The market place in consequence is enhanced by people of character. Not only that but people are by nature regarding as well as self-regarding. The opening sentence of Smith's *Theory of Moral Sentiments is, '*How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others, and render their happiness necessary to him, though he deserves nothing from it except the pleasure of seeing it!' It is because of this that a business must have at its core a purpose greater than profit. I find the idea of a greater purpose difficult to explore without regard to the values, beliefs and world view of its leaders. Profit is important but it is a means to an end, not an end in itself.

When someone decides to set up a business its purpose will reflect the beliefs and world view of its founder(s). These may differ widely because they reflect a different understanding of issues such as the dignity to which a person should be entitled, the nature of our responsibility for the environment, what constitutes fairness in compensation and promotion and so on.

I personally began to understand the importance of the purpose of business as a result of being a board member for many years of two American companies. One was Herman Miller, a public company quoted on the Nasdaq which produces office furniture. It was a design leader in the twentieth century and employed great designers such as Gilbert Rhode, George Nelson, Charles Eames, Alexander Girard, Isamu Noguchi and more recently Robert Propst and Bill Stumpf. Chairs which were produced in the nineteen fifties, such as the Eames lounge and Ottoman, seating and stools for the Time Life Building in New York and Noguchi coffee tables remain design classics and Action Office which was developed by the firm was the first open plan office in the US which revolutionised office space.

The Chairman and Chief Executive Officer who appointed me was Max de Pree who wrestled with the purpose of business. In reflecting on the purpose of business, Nicholas Woltersdorf, emeritus professor of philosophical theology at Yale, records attending an unusual all day chaired session by de Pree.

About ten years ago now I served – quite amazingly – as a philosophical consultant to the Herman Miller Furniture Company in Zeeland, Michigan. Max de Pree, the executive officer of the company had invited an architect, a physician, a journalist, a furniture designer, a theologian, and me to an all day session with him and about five of the top officers in his company. At the beginning of the day he posed ten questions that he wanted us to discuss, in whatever order we wished. He asked us not to concern ourselves with trying to say things that we thought would be useful to the company; he wanted the discussion to take whatever shape it wanted to take. I remember three of the questions. 'What is the purpose of business?' he asked. Some of his younger executives were saying that the purpose of business was to make money. He himself didn't believe that; but he wanted to talk about it. Second he wondered whether there was 'a moral imperative, ' as he called it, for companies to produce products of good design. And third, he wanted to discuss whether it was possible to preserve what he called 'intimacy' in a large company.

It became clear , in the course of the discussion, what de Pree himself regarded as the purpose of business. The purpose, as he saw it, was twofold: to produce products that serve a genuine need and are aesthetically good, and to provide meaningful work in pleasant surroundings for those employed in the company.

Now it seems to me that these two purposes are, or can be, an expression of charity – that is, both consist in concern to promote the welfare of the other. As a matter of fact, it became clear in the course of the discussion that it was de Pree's religious commitment – specifically, his Christian commitment – that had led him to embrace these goals. He saw his operation of the company as an exercise of charity – though he didn't use that word. His own case, at least as he presented it, was a case of 'transcendental faith' shaping economic activity.

When I joined the board of Servicemaster it was already a multi-billion dollar company, providing services in cleaning and pest control, publicly quoted on the NYSE, which employed and managed over 200,000 employees, serving six million customers in over thirty countries. It grew out of a culture similar to that of Quaker companies in the UK in the nineteenth century which seem in Europe like another country today. Servicemaster had four objectives; to honour God in all we do, to help people develop, to pursue excellence and to grow profitability. The first two were end goals, the second means goals. Harvard Business School wrote over a dozen case studies on the company and invariably the first objective always raised eyebrows as well as questions.

The chairman and chief executive of the company when I joined was C. William Pollard. He was at pains to explain that the company was not a religious company and had no religious affiliation. He commented on the link between the firms purpose and values in the context of growth: ' The first (objective) is meant to provide a starting point for all of us, not to convey a religious point of view. In combination with this second, if guides us by suggesting ways in which we treat people. The last two objectives not only provide the means for achieving the first two, they keep us in balance and provide a kind of creative tension for the management'. (Hesketh, James *The Culture Cycle* FT Press. 2012)

The ‘Can We? Should We?’ Test for New Business

The second challenge is the, ‘Can We? Should We?’ test for a piece of new business. A new piece of business for an investment bank can be varied. It may be an existing client wishing to make a hostile bid for another company, a former politician in an emerging market country wishing to transfer funds and open an account with private wealth management, a sovereign government needing to raise capital and offering as collateral a percentage of its gold reserves, the purchase of a bundle of mortgages from a retail bank which when securitised is sold on to high net worth clients, a business firm wishing to raise funds through a debt offering but which would make its outstanding debt to equity capital a high risk proposition.

The first test of any such piece of new business is that it must comply with the law and regulations issued by the regulatory authorities. Next it must be commercial. The bank must price the deal so that it covers its costs including the return to shareholders . When these two tests are passed, the first question – can we do this piece of business? – has been answered affirmatively. In the past the general principle for business conducted between competing financial institutions was *caveat emptor,* ‘let the buyer beware’. The assumption was that if firms were staffed by professionals with experience of the business they were conducting, they should know full well the risks they were taking in an individual transaction. This criterion never applied to retail customers because it was assumed they would be far less knowledge of the risks they were taking.

However there is a second question which banks must also ask themselves about a piece of business. Not can we do it? But should we do it? Is it the right thing to do? How damaging would be the reputational risk of the transaction? What if the transaction involved fees to the client, which if they were made public, would seem exorbitant? What if the transaction was opposed by an environmental lobby? Or involved significant redundancies? What if the purpose of the transaction was to avoid tax or circumvent regulation?

Reputational risk is extremely important to any business or bank. One of the fourteen business principles of Goldman Sachs states that, ‘Our assets are our people, capital and reputation. If any of these is ever diminished, the last is the most difficult to restore. We are dedicated to complying fully with the letter and spirit of the laws, rules and ethical principles that govern us. Our continued success depends upon unswerving adherence to this standard.’

One test for deciding whether or not to do a particular piece of business is what if it became headlines in the local newspaper or in the social media? How would children, family and friends respond? Another was set out by Dennis Weatherstone ex-CEO of JP Morgan. His dilemma was how to decide which new and obscure financial products which were being suggested by traders, mathematicians and quants the firm should sell to its clients. Weatherstone's tactic was to give to those creating these new products three slots of 15 minutes each to explain the products to him. If at the end he did not understand it JP Morgan would not sell it.

One way of implementing the 'should we?' test is to create a process around the decision regarding suitability, which is not the decision of one or two individuals, but involving a vetting group drawn from both the revenue creation and the control side of the firm. The deal may still go ahead as proposed, but such a structure will help ensure that the transaction will have been thoroughly examined.

Work/Life Balance

A third issue is work life balance. 'The pressure of an increasingly demanding work culture in the UK is perhaps the biggest and most pressing challenge to the mental health of the general population. The cumulative effect of increased working hours is having an important effect on the lifestyle of a high number f people which is likely to prove damaging to their mental well-being'. (Mental Health Foundation).

Work related stress costs Britain 10.4million working days per year. Research studies suggest that over 25% of the workforce face challenges regarding their work life balance. A Mental Health Foundation survey found that 40% of employees are neglecting other aspects of their life because of work. When working long hours more than 25% feel depressed. The more hours spent at work, the more time spent worrying about it when not at work. Nearly two thirds of employees replied that an excessive work load damaged relationships and home life.

One factor making for an increasingly demanding work culture in recent decades has been the increasing competitiveness facing companies because of the continued disruptive effects of globalisation, technological change, longer opening hours for retail stores including weekends, increased migration of labour, deregulation and a reduction in the power of trade unions. The increasing pressures from increased competition are the real time demands of information technology, the need for a speedy response, the quality offered for customer service and the need for availability and the pace of change in the work place. As a result more pressure is placed on employers because of greater employee turnover, stress, reduced job satisfaction and lower productivity.
In terms of tackling the problem two factors are important. One is for companies to introduce flexible working options: flexitime, annualised hours, term time working, shift working, rota working/staggered hours, job share, job splits, part time working, flexible retirement, remote working, compressed hours, career breaks. Not all of these are possible in all jobs but flexible working options can help reduce the problem of imbalance. A second factor is the support of the line manager, which turns out to be a key factor.

It is not uncommon for people in the highly competitive world of financial services – bankers, traders, lawyers, accountants – to work extremely long hours. Some reports have suggested that bankers in certain areas, such as mergers and acquisitions, typically work from 9am to midnight five days a week and even into the weekend. The issue of long hours came to a head in August 2013 when in the City of London a 21 year old intern at Merrill Lynch died after allegedly working until 6am for three consecutive nights. It was not clear that the hours worked were the cause of death, but it was a wake-up call for banks. Most have responded by restricting the hours interns work. For example Goldman Sachs set a maximum of 17 hours a day and introduced a Saturday Rule stating that, all analysts and associates are required to be out of the office from 9pm on Friday until 9am on Sunday. Exceptions might be necessary if a deal was time sensitive but the expectation should be that work assigned on a Saturday would not be expected to be completed on a Saturday.

Whistleblowing

A whistleblower is someone working within an organisation who exposes wrongdoing which could be illegal, unethical or a violation of company rules. This may relate to any business conduct issue. Whistleblowers may refer their concerns to their immediate line managers. Or they may prefer to use an internal process which guards anonymity. Many firms now have a hot line to an external number which again guarantees anonymity. Some may go public by contacting the media or the police. Complaints which are categorised as whistleblowing tend to be in the public interest rather than personal grievances over pay, promotion, harassment, bullying or discrimination.

Whistleblowers take great personal risk. Whistleblowing is easily viewed as letting the team down, breaching confidentiality and displaying disloyalty. Whistleblowing requires courage. Back in 2002 Sheron Watkins who was then a vice president of corporate development at Enron and who had worked at the firm for 9 years alerted the then CEO, Ken Lay to accounting irregularities in its financial reports. Previously she had worked for 8 years as an auditor with accounting firm Arthur Andersen. Her whistleblowing was one factor that led to the collapse of Enron and Arthur Andersen and sent Kenneth Lay and other Enron executives to prison. She recorded her experience in her book *Power Failure: the Inside Story of the Collapse of Enron (2004).*

Speaking a decade later at the *Beyond Rubicon* conference in Cedar Rapids she said that she would do it again but she would not do it alone: 'If you want to have the courage of your convictions you have to safeguard your reputation. I could take risk because I didn't have any skeletons in my closet…..Most people think they'll do the right thing. If you see unethical practices at your company your career is forever changed. You're either going along with it or protesting and being labelled a trouble maker.'

Paul Moore was a whistleblower in HBOS, which was the UK's largest mortgage provider. He was head of group regulatory risk. (Alex Hawkes, Financial Mail on Sunday, 21 November 2015). HBOS ran into financial difficulties. It was bailed out by the government in October 2008, bought by Lloyds Bank in 2009 which subsequently need a £20.5billion cash injection from taxpayers to prevent its collapse. Moore published a book *'Bang, Crash, Wallop' (New Wilberforce media 2015)* and has since said, 'If I had known the misery it would cause I wouldn't have had the courage to do it.' His excessive drinking and deterioration of mental health became serious problems. It was he said only his faith and the solidarity of his wife which got him through.

Because of the risks whistleblowers face, employers need to offer clear avenues by which they can express their concerns with total confidentiality and, if necessary, anonymity. They also need to be assured that there will be no retaliation against them should their complaints prove unfounded.

We have no reliable evidence on the extent of whistleblowing but it would seem that, for understandable reasons, few employees resort to it. However there are certain cases where it would seem a significant number of people have known of wrongdoing taking place but did nothing. Wells Fargo, the Californian bank has faced a series of scandals since 2016. It would seem that because employees faced unrelenting pressure to meet sales targets staff unlawfully opened accounts and misled the public about fraudulent practices at the bank. The judge handling the case commented that because there was a pervasive and undisputed fraud at the core of the company's business, "…it is reasonable to infer that senior executives knew about, or at least recklessly turned a blind eye to, the stream of red flags."

One question in relation to whistleblowing is whether firms or regulators should be prepared to compensate whistleblowers. In the UK the FCA has said it will not pay. In the US the SEC has started to pay.

Conflicts of Interest

A conflict of interest is an incentive, apparent or actual, to serve one interest at the expense of another interest or obligation. Professor John Kay, a hugely respected commentator on the financial system, has argued that 'investment banks today engage in securities issuance, corporate advice and asset management: they make markets in equities and FICC (fixed income, currencies and commodities), and trade in these markets on their own account. It is only necessary to list these functions to see that each of these activities conflicts with all the others.'

Examples of conflicts would be advising clients on both sides of a transaction, withholding valuation information until very late in a transaction, mischaracterising projections as representing Wall Street consensus, not disclosing prior relationships with another company to a potential client, using information as a market maker, to trade on its own account ahead of clients and so on. Because of the widespread nature of conflicts of interest in financial markets one approach is to argue that each of the activities undertaken by investment banks should be undertaken in separate institutions. This was the case in the US for the Glass-Seagull Act (1933) which separated commercial and investment banking and the Dodd-Frank Wall Street Reform and Consumer Protection Act (2010) which prohibits investment banks from carrying out certain activities (Volcker Rule, merchant banking). In the UK and the EU there has been a huge unease in regulation but little prohibition as in the US.

Even when activities are separated and regulation extended, as has happened since the 2008 financial crisis, conflicts of interest still remain. The challenge for institutions is how conflicts can be managed for individuals working in the institutions to be clear as to the basis of their personal judgements. Every bank needs a conflicts of resolution group of executives which examines whether a piece of new business is in conflict with exiting business commitments or historic roles the firm may have played and which are relevant, or existing positions held by various parts of the firm as well as potential client sensitivities. Others in the group should also consider whether certain actions could help such as disclosure, release from prior roles and special restrictions placed on information sharing between different teams. Documentation is important especially in relation to disclosures made to clients, separating information between teams for strategic assignation and check as to whether the relevant area of the firm may be in possession of material, non-public information or price sensitive information relevant to the transaction.