G R E S H A M

C O L L E G E

ETHICAL CHOICES IN BUSINESS

Three lectures given by

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Lecture 1 - 5 March 1991
CONFLICTS OF LOYALTY

Lecture 2 - 19 March 1991
ADVERTISING AND SPONSORSHIP

Lecture 3 - 26 March 1991
ETHICS AUDITING

GRESHAM COLLEGE

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GRESHAM COLLEGE

THREE PUBLIC LECTURES

on

ETHICAL CHOICES IN BUSINESS

by The Revd Professor
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Mercers' School Memorial Professor of Commerce at
Gresham College

delivered at the Parish Church
of St Edmund the King
Lombard St London EC3

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I Conflicts of Loyalty
II Advertising & Sponsorship
III Ethics Auditing

CONFLICTS OF LOYALTY

Some of the most teasing problems in the ethical conduct of business consist in conflicts of loyalty, or conflicts between loyalties, as between loyalty to one's company or colleagues and loyalty to the wider community, society, or to the truth or one's personal ethical standards or principles. And in exploring this area of conflicts of loyalty it may help to begin by considering the wider and more common context of conflicts of interest.

I

When the subject of conflicts of interests arises it is most commonly connected with one's personal interest, and the tension which can occur between that and the interests of a larger body to which one belongs. A good instance of awareness of potential conflict of interest is the move in the House of Commons for members to register their business connections or directorships, so that it is clear when they may have a 'vested interest', or an ulterior motive, when they are exerting an influence on legislation which is ostensibly aimed to promote the public interest. In committee work it is common practice also when one is making a point or arguing a case, to 'declare an interest' if one has one in the subject under consideration. And it frequently occurs in correspondence columns of newspapers that below the signature of, e.g., someone trumpeting the obvious and superior merits of cycling over other forms of urban transport, it is made clear that the correspondent happens to be chairman of a large company of bicycle manufacturers.

One central issue of the situation of potential conflicts of interest may be summed up in that phrase 'happens to be', which draws attention to a particular factor or relevant feature of the situation. The ethical question which this raises is how that factor influences the outcome of a developing situation. If I am discussing exactly how Mozart died, for instance, or whether Bacon wrote Shakespeare, and 'it so happens' that I am the world authority on the history of public health in Vienna, or on sixteenth-century English literary style, then, on the face of it, this may be advantageous to the final outcome of the discussion and to the advancement of public knowledge. But by the same token, if one of my research students discovers a signed confession by Salieri that he poisoned Mozart, or incontrovertible proof that Bacon couldn't possibly have written *King Lear*, and these are at variance with my own views on the matter, then the temptation for me may be to suppress such findings and to safeguard my own interests, reputation and royalties, at the expense of the interests of scholarship or of the public interest. Perhaps what these cases help to bring out is the useful distinction between potential conflicts of interest and actual conflicts of interest, or the difference between opportunities for individuals to abuse their position, and the actual abuse to which they may succumb.

I suppose a good medical illustration of the idea of a conflict of interests may be cancer, where a cell of the body whose function is to fit into and contribute to the general physical equilibrium and harmony of the body turns rogue and proliferates in the body, diverting the body's material and purposes to its own interests and aggrandisement. And this idea of an organism, or even of an organisation, may help to provide a general overall framework within which to consider the idea of conflict of interests. The danger is evidently one of abusing one's position of power or of privilege within a community or an organisation. And the particular form which the abuse of power takes is to divert the organisation from its stated objectives, in order to promote and favour the objectives of only part of the organisation, or of a minority within the organisation, including a minority of one.

II

The idea most commonly associated with the issue of conflict of interests is that of private, personal gain, and this can take many forms which I need not elaborate. It may be in terms of direct financial gain, as in insider trading or accepting bribes or private *quid pro quo*'s. Or it may be in terms of using one's official position or authority or the facilities of one's position for purely personal purposes, such as nepotism or favouritism, or engaging in personal vendettas, or empire-building.

An interesting situation can arise, however, when a conflict of interests exists not between an individual in his or her private capacity and the organisation, but actually within the organisation. In much of the activity and discussion connected in recent years with company mergers and acquisitions, often the spotlight was focused on management, and to what extent its moves either to welcome or to repel potential boarders were in the best interests of the company, or more truthfully were only in their own sectoral interests, to the detriment of the company.

Again, the well-known phenomenon of 'short-termism' on the part of institutional investors is viewed by many as a conflict of interests between those primarily concerned to maximise their funds and those more concerned with the long-term wellbeing of the company. And within the working organisation it is possible for separate divisions or departments to pursue their own particular interests apparently at the expense of other divisions or departments, or even at the expense of the company as a whole. One example sometimes referred to is the bullish activity of sales personnel to meet targets by making promises of delivery or performance which cannot in fact be met by production.

III

In all such cases of sectoral interests the general ethical presumption is that the interests of the organisation as a whole should prevail over the interests of individuals or of parts of the organisation. And this primacy accorded to the organisation as a whole is often expressed in terms of the idea and the ethical claims of loyalty. Yet there are some issues which should perhaps make us wary of simply accepting this idea of corporate loyalty as an ethical absolute. One, for example, can arise in connection with safety considerations, where the research and development experts may consider that not enough time or resources have been given to thoroughly testing a new product for which distributors and customers may be clamouring, whether it be a new wonder drug or a children's toy or a car with a fabulous new fuel system. In its extreme form such conflict of interest may even find expression in whistleblowing, if those within the organisation who are knowledgeable and concerned fear that their genuine reservations about safety are being swept aside in the global interests of company sales and profit. It is considerations such as these which indicate that conflicts of interest may not be simply self-serving conflicts between personal and corporate interests, but may on occasion be conflicts between corporate interests and the public interest. And in such situations the choice becomes not one between loyalty and disloyalty to one's organisation. It becomes a conflict of loyalties, with the choice to be made between loyalty to one's employer or organisation and loyalty to the wider body of society.

A second issue which prompts one to qualify the idea of unquestioned loyalty to the interests of the organisation arises from not just safety, or public, considerations, but from professional considerations, on the part of members of, for instance, the financial, legal or medical professions whose services are used by the organisation. In such instances the potential and actual conflicts of interest may come down to a matter of professional integrity, where loyalty to a client or an employer can become more a matter of collusion. It may be argued in such instances, of course, as in the case of whistleblowing, that declining to subscribe absolutely to the present or immediate interests of the organisation is in fact acting in its long-term interests or in accordance with its true objectives. Putting the conflict in these terms can be seen as one expression of the debateable maxim that good ethics is good business, which, as I have observed on an earlier occasion, is sufficiently true to be dangerous.

A more productive way of viewing such professional considerations seems to lie in the light which it throws on the whole question of organisational loyalty within society. If one can accept, at least *prima facie*, that the prevailing loyalty of individuals and parts within the organisation is to the objectives of the organisation, then by the same principle one can logically argue that the prevailing loyalty of the organisation itself lies within the context of the wider social body of which it itself is only a part. From which it follows that in business when there is a potential conflict of interests between the organisation and the public interest, it is the latter which should always take precedence over any sectoral interest. And this applies, of course, not just in home markets, but particularly and sensitively also in foreign markets.

In one respect the whole subject of conflicts of interest in business is a particular expression of the 'stakeholder' theory of business, for it is evident that the various parties who come together in the activity of an organisation each have their own portfolio of individual interests. People are not one-dimensional, but multi-dimensional; and that is what makes them so interesting. Coming together to find some measure of overlapping interests in an organisation does not necessarily depreciate the interests which one does not share with others on that occasion. But it does cast a light on those other interests and on their relevance or propriety within the context of agreed shared interests. And the received wisdom has identified various ways in which such extraneous interests should be regarded and treated.

The most important is probably transparency, disclosure, or publicly available information. Not that this necessarily entails that an individual will not seek to promote his or her own agenda in ostensibly collaborating with others. But at least it prevents it from being a private or hidden agenda, and alerts others to the possibility of ulterior motives, as well as having a cautionary influence on the individual concerned. Such transparency is one method of reducing the potential for conflict of interests, but another may be simply the prohibiting of certain activities being carried on concurrently, either by regulation on the part of the organisation or as a legal enactment. And here the motive appears to be not so much to inform others of a potential conflict of interests as to dispel the temptation or even the appearance of abusing one's position.

It could be, and has been, argued, of course, that such policies argue a pessimistic view of human nature and discriminate by excluding from certain business activities those individuals of robust moral character who have much of value to contribute to it. On the other hand, it may be claimed that sad experience makes such rules necessary, and that it is, on the whole, better to be safe than sorry. At any rate, it is noteworthy that most, if not all, company codes of practice make particular mention of the dangers of individual conflicts of interest and of the steps to be taken to ensure that they do not materialise.

By way of conclusion, then, let me suggest that not all conflicts of interest in business are necessarily undesirable. What perhaps they may point to, at best, is the existence of tensions which are to be found within all joint human enterprises precisely because such enterprises involve only a partial overlap of personal or group interests. Within professions such as the law, medicine, and the church, such tensions may be viewed as in the nature of professional hazards. And ultimately within business too, for all the safeguards which may be introduced or applied, the only satisfactory approach to the subject must be the personal integrity of the individual, and the spirit of professionalism which he and she bring to their function and role not just in the organisation, but in the wider society of which the organisation is an integral part. As so often in the whole field of business ethics, we seem to be basically considering the ethics of power, and in this instance the ethics of examining whether, and under what conditions, the power which comes from belonging to one sphere of action and whose *raison d'etre* is to promote that sphere of action can be utilised in other areas of one's life, often to the detriment of the sphere within which the power first arises.

ADVERTISING AND SPONSORSHIP

Dr Johnson once wrote that 'Promise, large promise, is the soul of an advertisement.' And I suppose that alerts us as well as any other description of advertising to what might be regarded in summary as the major ethical aspects of advertising: Should advertising make the promises it does make? And does it deliver on its promises?

I

The economic case for advertising is fairly clear when it is considered as a necessary component of the competitive market system. It draws attention to goods and services which are available, and by stimulating purchases it contributes to a return on costs, increases the market share of products, leads to increased production and reduction of unit costs, and in general contributes to a better material standard of living all round. In this sense advertising may be considered inherently good, and a valuable element of the conduct of business in a free society.

From a fuller human perspective advertising also contributes to an expansion of human freedom, by increasing the scope and the range of people's choices, and enabling them to satisfy their desires and to enhance the quality of their living. When the Berlin Wall was broken through and East Berliners flocked wide-eyed into the glitter of West Berlin and its shop-windows, they became aware of the sheer poverty of choice under which they had laboured for years, and of the diminished freedom, not just economic but also in human terms, from which they were breaking free. I do not wish to be considered starry-eyed about either the capitalist system or the conditions of the market economy, and I shall shortly turn to consider the failings of advertising as it is sometimes or frequently practised. My main introductory point, however, is to propose that in principle advertising is a desirable and valuable feature of society, in bringing together demand and supply by means of communication and in enabling individuals to exercise their freedom of choice and enhance their personal freedom in many new and often different ways.

I have referred to advertising as a communication, and that is what it basically is. It is not, of course, disinterested communication, in terms of truth for truth's sake, or the dissemination of information in purely altruistic terms; and therein lie many of the ethical issues involved in advertising. It is communication with a vested interest, presenting information with a view to sales, and in legal terms setting up the situation for a contract in commutative justice. As such a relationship between persons, either in their own capacity or as agents for others, the communication involved in advertising is therefore subject to various ethical conditions which affect the way in which people treat each other. And one important ethical condition is the way in which people respect each others' freedom, including their freedom to make rational and informed choices.

In the particular communication of advertising the basic tension may be considered to be that the potential customer seeks information in order to make a choice, while the potential seller seeks to persuade in order to make a sale. The danger is then that the seller's motive to exercise influence, with a view to competing with other sellers or just to increasing turnover, may lead him or her to short-change the potential customer in one of two ways, either in the information provided or in the pressure brought to bear in various ways on the customer. I propose to consider each of these ideas of information and pressure in turn.

II

If we consider information, then what this brings out is that human freedom, to be truly human, has to be informed, or knowledgeable, freedom. It is not simply the exercise of arbitrary decisions; it is based on factual and rational considerations. In the field of medicine, for example, signing a consent form for treatment is not, or should not be, merely a bureaucratic formality. It involves the basic idea of informed consent; consent, that is, which shows an awareness of what is involved in the treatment, of what is the hoped for outcome, and of what are the likely hazards which may also be encountered along the way.

Similar conditions affect the buying of other goods and services in society. And this is where the whole question of truth comes into the picture of advertising, as a necessary condition of our choices not being vitiated by ignorance or biased by deception. I need not labour the general point about the need for claims about a product to be accurate and truthful, and not to suffer from lying or misrepresentation. At the level of application, however, to particular cases or practices in advertising several counter-claims have to be considered. For instance, there may be a gray area in the distinction between, on the one hand, misrepresentation, or making claims which are false, and on the other hand omitting certain facts about the product, or being, in the now famous phrase, 'economical with the truth'. While singing the praises of a product does one necessarily need to point out all its failings and weaknesses? Perhaps it may suffice to say in general terms that ethically the potential customer has a right to whatever information is considered relevant and necessary for him or her to make a free and rational choice; and that this will include his or her being made aware of those particular features which, were they known, would materially affect that choice: for instance, that the machinery is dangerous, or that spare parts will shortly go out of production, or that the rate of interest can be changed at will by the creditor, or that between the luxury time-sharing block of flats and the glistening sands there are plans to build a new eight-lane motorway.

Exaggerations and unwarranted claims about the efficacy of the product also fall into consideration in assessing the truth factor in advertising, whether those claims have to do with one's health, or one's sex appeal, or one's social status, or one's general wellbeing in society. The counter to such considerations may often be that there's nothing wrong with a little harmless exaggeration, that no one is really fooled by it, and that in any case there is considerable scepticism which has to be taken into account. A too punctilious or solemn approach to advertisements would take all the fun and attractiveness out of them, reducing them to a mere scrupulous cataloguing of sales features. Surely no one is fooled by the pictorial element in advertisements, whether it be the use of mashed potatoes in place of the ice-cream which would melt under the arc-lights, or the sight of a new razor in action effortlessly removing the surface from a sheet of sandpaper.

It must be acknowledged that there are certain conventions in this form of communication, as in every other, whether it be bluffing in the course of agreeing a price or a wage rate, or obviously outlandish suggestions that drinking a special brand of vodka will transport one into a fairyland or harem of delights. The unspoken presupposition here, of course, is that the potential customer will be not only resistent but also sensible and reasonable in assessing the claims for various goods and services and will not take it all absolutely literally. The problem lies with the concept or the criterion of the 'reasonable consumer' which is appealed to. Certain levels of intelligence may no doubt be taken for granted in some cases, but there are particular problems at least in the case of some groups in society, such as young children, adolescents and others who may feel socially inadequate, people in poor health, or individuals suffering from addictions of various kinds. In all of these and others there is an element not just of needs to be met or wants to be satisfied, but of vulnerability, which is exploited by inflated claims for what a particular product will deliver.

It is in such areas particularly that regulation and monitoring of advertisements have an important social function by protecting the vulnerable in society from being exploited. But in ethical terms what should be most to the fore on the part of advertisers is not just compliance with the letter of the law or regulation, perhaps coupled with attempts to get round it or slip past it, but the spirit of the law. And that is based on a fundamental respect for consumers as primarily human beings and not just potential customers, an awareness of their need for relevant information in order to exercise their freedom of choice, and an alertness to their human vulnerability, as contrasted with their rational needs and desires.

III

The second and perhaps more ethically interesting sphere in which advertising needs to be scrutinised, is the area of pressure on individuals to make particular choices, to which I now turn. For not only is freedom dependent on accuracy of information in the ways in which I have been suggesting; it is also dependent on immunity from undue pressure. And in that simple phrase 'undue pressure' there are many important considerations to be unpacked and analysed.

The ultimate assault on the freedom of a potential customer is generally agreed to be the activity of subliminal persuasion, and it is interesting to explore just why such extreme advertising techniques are considered ethically wrong. In part it appears to be because the approach slips through the consciousness of the subject, as it were, so that, in the popular phrase, they are 'being got at' without their permission. In that sense subliminal advertising may be considered an invasion of psychic privacy. Additionally, however, what is also involved in such techniques is that they bypass one's exercise of rationality and seek to influence one's choices by a direct appeal to feelings and emotions. We may recall Aristotle's comment that human beings are characteristically rational animals, and if that is so, then we may conclude in general that any attempt to influence people's choices in irrational or non-rational ways is ultimately demeaning to them and to their dignity as rational human beings.

Feelings and emotions do, of course, have a place in ordinary human decisions. We are not calculators, nor do we always fulfil the economic expectation of being entirely intellectual and predictable in our choices. And this raises the ethical question of how far advertising can justifiably play on our feelings and emotions in order to influence our choices. As Dr Johnson observed, in my opening quotation, 'Promise, large promise, is the soul of an advertisement.' And you may recall Vance Packard's remark in his perhaps over-sensational study of *The Hidden Persuaders* that shoe-shops do not sell ladies' shoes; they sell 'beautiful feet.' What Packard and others object to is not persuasion on the part of the salesforce, but hidden persuasion, of which the potential customer is unaware.

There appears to be nothing wrong with persuasion as such: most of us are doing it much of the time in our attempts to bring others round to our way of thinking. In the Introduction to his famous Essay *On Liberty* John Stuart Mill attacked the idea of compelling others to behave in certain ways because it would make then happier or better or wiser people, or even right, and he explained, 'there are good reasons for remonstrating with him, or reasoning with him, or persuading him, or entreating him, but not for compelling him', although he carefully made exceptions in the case of minors and 'backwards states of society'. I suppose the point here is that, for persuasion to be legitimate it must be rational or at least amenable to rational consideration. And in this context it seems ethically permissible to attempt to persuade others by appealing not only to individual arguments leading to choices but also to individuals' motives in approaching their choices.

One of the problems, however, remains to what extent such appeal to personal motivation actually is amenable to rational consideration, and for that we have to be conscious of such appeals rather than let them slip under our guard. Ultimately perhaps this is the difference between persuasion and manipulation, in what I suggest may be a sliding scale of information, suggestion, persuasion and manipulation. Information here may be seen as simply the offering of the possibility of satisfying a person's felt and acknowledged want: You want a mousetrap? I sell mousetraps. Suggestion may be more a matter of helping the customer to articulate his or her desire: Wouldn't it be nice to get away from it all? Have you considered whether you need a weekend break? Persuasion may consist in marshalling the arguments for buying the latest encyclopaedia or shares in the new government privatisation. All of these include the element of rational consideration, although of course it need not be in verbal propositions; it can also be conveyed more subtly and attractively in visual terms. And inevitably all of these also contain a strong element of attraction, since in our choices of goods and services we are aiming not just at what is true and appeals to our mind, but primarily at what is good and what we should like to have or obtain. By contrast with all of these, manipulation consists in getting people to make decisions and choices without their actually being aware of why they decide or choose in this manner.

There is one final and underlying consideration concerning the ethics of advertising which I want to look at briefly before turning to the question of sponsorship, and that is to what extent advertising responds to demand or on the contrary actually creates demands. The thesis is well known that the purpose of advertising is to create dissatisfaction, so that potential customers who may have been blithely unaware of the range of products and services available are enticed into purchasing them without actually needing them. Perhaps the most obvious instance here, apart from so-called 'luxury goods', are various addictive or dependency-inducing substances such as tobacco and alcohol. And national and European regulation limiting advertising in these areas appears partly directed at preventing the market from growing by stimulating sales. More serious perhaps is the creation of new customers for the arms trade.

Part of an answer to this charge against advertising is economic in nature, that costs have to be recovered, or that a given volume of sales is essential to justifying R & D, as in the development of new armaments, and that the only way of achieving this is by increasing the market. In more psychological terms, however, the charge presumes that new human needs should not be created, and that we should all be content with satisfying our basic requirements in society. It is not easy, however, to distinguish between human needs, wants, and desires. Perhaps needs are deepest, and are expressed or consciously articulated in wants, while desires refer to less significant or less profound experiences. Perhaps also this is where the distinction which I have already suggested between information and suggestion is important, insofar as suggestion can articulate in terms of wants what is already an underlying unconscious need.

More fundamentally, however, the attempt to distinguish between basic needs and perhaps induced needs, while important when sheer human survival is concerned, becomes less successful when quality of life and human culture are concerned. I have always remembered a TV play of Marghanita Laski called, if I recall, *The Offshore Island*, in which Britain had been devastated by nuclear disaster and a mother was concerned not only to feed her children but also to teach them to sing the theme from Beethoven's *Choral Symphony*, so that good music would not be entirely lost. Part of human culture, then, consists in inducting people into new experiences, perhaps largely of an aesthetic kind and to do with the human senses, and in the process creating habits and even needs which then fall to be satisfied. If this is the case, the conspiracy charge against advertising in general must be considered not proven, even if in particular instances it may well be sustained.

Perhaps, however, a final general point may be raised about advertising in general, and that concerns the values which it promotes, either covertly or even overtly. The cultural stereotypes of gleaming fitted kitchens, or of female or male sex-objects, are not only holding out promises of a vague kind; they are also inculcating views of life and of human relationships in society which often give serious cause for ethical questioning, if not disquiet. It may be easy here, of course, to confuse taste with ethics, but the depiction of reality in shocking or seductive or otherwise offensive terms may be matter for considering whether mental or cultural health warnings should sometimes accompany some advertisements.

IV

My title also includes the ethics of sponsorship, and here there has, I think, been rather less thought given to the subject than in the case of advertising. Perhaps here I ought to declare an interest, because my Business Ethics Centre in King's College London is currently seeking sponsorship for a Conference on European Business Ethics which we are hosting in London this September.

In general terms sponsorship is often expressed as the exercise of corporate responsibility or of corporate generosity towards the community, and there appears nothing exceptionable in this, and much to commend it. Again, of course, it can scarcely be termed purely altruistic, since the company expects some return in goodwill and popularity, and even in some cases gratitude, if the event or the institution might not otherwise exist or be provided. The standard arguments against corporate giving can apply here, to the extent that individual shareholders might prefer to make their own philanthropic decisions rather than have them made for them by others. But I suppose one counter-argument, at least so far as the beneficiaries are concerned, is that the amount contributed will be the greater if it is exercised at corporate level. Another difficulty can concern the choice of 'good causes' as the recipients of corporate generosity: on what criteria they are decided, by whom, and with what background of expertise and experience to exercise discrimination.

It is also noteworthy, of course, that some sponsorship is actually advertising by association on the part of companies whose direct advertising of particular products may be limited or curtailed. This is where the difference between advertising particular products and drawing public attention to the company's image as a whole by sponsorship is ethically relevant, for such indirect advertising may be an attempt to evade laws or regulations according to their letter, although it clearly contravenes the spirit and the social purpose of such enactments. Again, some sponsorship may be an attempt to make amends, or even to induce the public to overlook other perhaps more undesirable features of the company or its products.

Whether, however, in conclusion, we address the subject of sponsorship or of advertising there is no doubt that they raise for serious consideration many ethical questions which extend well beyond the economic arguments. They influence and affect our views of society, of human relationships, of our use of material possessions, and of human communication. Ultimately, all such considerations appear to come down to what Kant referred to in considering our attitude to others, that in all our dealings we should treat each other as ends and never merely as means. Of course, in many ways we are always treating others partly as means - that is to some extent what business is significantly about. But to consider others simply and solely as potential sales and to regard their rational freedom as negotiable in the enterprise of making sales is to depersonalise them and to deprive them of their basic humanity and dignity as persons.

ETHICS AUDITING

As interest in the ethical conduct of business arises and begins to develop, there is one basic question which eventually emerges. Should ethical considerations in business be an occasional or sporadic interest for any company, depending on the pressures coming from outside the company or on the concern of one or more individuals within the firm? Or should a concern for ethical consistency in the company's activities be institutionalised in some way or other within the company? In previous Gresham lectures I have explored such corporate ethical institutions as mission statements and company codes of conduct, as well as the possible introduction of ethics committees or ombudsmen, and the identifying of a specifically ethical role for non-executive directors in a company. What I want to explore in this lecture is the possibility of introducing a regular internal review of a company's ethical performance, drawing on its ethical monitoring in the course of the past year and providing an annual opportunity for the company to appraise the ethical quality of all its activities.

In some respects the idea of an ethics audit is not a new one. The 1970s, for example, saw serious exploration in the United States of the idea of a corporate social audit; during the 1980s the idea developed and has caught on of a regular corporate environmental audit; and for the 1990s some writers foresee a demand and a practice growing of 'corporate social and environmental accounting'. In this last lecture of my series on *Ethical Choices in Business* I propose to trace the developments of these ideas, and consider their strengths and weaknesses, before proposing for consideration and adoption by business firms the idea of an Annual Company Ethics Review.

I

The idea of corporate social auditing rose into prominence in the United States as part of the move on the part of businesses to respond to growing social pressures on them to meet new and rising expectations and responsibilities. Basically the aim was to take as a model the regular financial auditing and the production of an annual financial report, to which businesses were accustomed, and to produce an audit of the company's social activities and thus present its annual report of corporate social involvement. Initially, the idea of such a corporate social audit was greeted with enthusiasm as a means of manifesting the company's record of citizenship and social involvement, and various schemes and social spreadsheets were devised and introduced in order to itemise and assess the company's record. These covered such entries as community involvement, whether in terms of financial gifts or of personnel time, avoidance of discrimination in employment, health and safety programmes for employees, consumer protection and other services, coping with accidents and faulty products, and so on. And the model of financial accounting was further applied in sustained attempts to quantify, measure and report on all these activities of the corporation.

And there, of course, lay the two major difficulties of the social audit movement: how to conduct the auditing process in terms of some basic unit of calculation; and the underlying assumptions of applying cost-benefit analysis to the company's record of its social behaviour. In terms of costs and expenditure it is possible to quantify in financial terms some social commitment on the part of a company, as in the amount of money allocated annually to community involvement, either in terms of outright gifts or in terms of the man-hours involved in officially seconding or appointing personnel to such activities. But it proved more difficult to make social capital out of spare-time or off-site involvement in the community on the part of company staff. Equally it is comparatively simple to estimate the costs of putting new programmes in place to deal with health and safety in the work environment, or to cope with customer complaints, or to adopt a production policy of 'total quality'. And perhaps it is possible to some extent to quantify improved working conditions in terms of fewer accidents or increased output, or to verify consumer and public satisfaction in terms of steady or improved sales figures. But in the wider social context how does one measure the financial effect of a policy of affirmative action in employment and promotion, or the beneficial results to the local community stemming from an improved programme of waste disposal. More generally, what time scale is one using to assess the return effects for the company of these and other forms of socially responsible behaviour?

In other words, while it may be possible to quantify in financial terms some or many of the costs incurred by a company in adopting a programme of social responsibility, it does not appear very practicable to identify and quantify the benefits which may result. One reason for this is because of the difficulty of identifying whose benefits one is considering, and whether these are the benefit to the public at large, or to, for example, the work force, or to the company itself. And if the social audit exercise is one which inevitably concentrates on producing a balance sheet for the company, then either its focus is inevitably too narrow, concentrating on its own benefit, or there are going to be many large gaps or wild guesses on the credit side. The principle on which Jeremy Bentham's theory of utilitarian calculation was based, and foundered, was that there are basic units of human pleasure, or satisfaction, which can be identified and quantified, in order to be compared and traded off in ethical decision-making. In a similar manner, one of the major problems of using cost-benefit analysis in the bid to audit a company's social performance is the frequently expressed objection that there are some things in life which simply cannot be quantified or measured, such as freedom, aesthetic satisfaction, fresh air, immunity from harm, or general individual or social wellbeing.

In partial defence of social auditing, however, it is sometimes pointed out that its aims are more modest than that. It is not concerned with *whether* a company should adopt a programme of positive social responsibility, but simply with *how* it should do so, once it has decided to adopt such a programme. In other words, it aims to measure performance in achieving certain pre-selected goals, by assessing alternative methods of achieving those goals and attempting to identify the most efficient and cost-effective manner of proceeding. And yet, important as this must be in scrutinising costs and in placing a brake on the temptation to throw money at social problems, the difficulty remains of identifying what is to count as success, how to identify it, and what means to devise of quantifying it in order to offset the resulting calculations against costs. In a word, is it at all useful to use the tools of financial accountancy in an attempt to measure moral accountability?

II

Given the theoretical difficulties, and perhaps particularly the sheer practical difficulties of operating and producing a corporate social audit along the lines I have described, it is not surprising that after some initial enthusiasm this particular exercise in corporate social responsibility began to lose favour and support. However, the whole idea of auditing other activities of the company besides its financial performance was given a fresh impetus with the rise and growing popularity of concern for the environment. And during the 1980s the idea of conducting a regular environmental audit of businesses grew in favour and is becoming popular. In the United States its first purpose was to scrutinise a company's compliance with government and other regulations in the specific areas of waste disposal and pollution, and this spilled over to American overseas subsidiaries, where it also met in Britain, for example, not so much regulation as growing environmental sensitivity on the part of the public. At first the concentration was on checking company locations of sites and plants, but in due course this extended to include testing its manufacturing processes and products. Now the idea of environmental auditing is envisaged also as covering a 'cradle to grave' approach to a company's products, in monitoring the various stages of its life cycle, ranging from the choice, source and securing of its raw materials, to the efficient and safe application of energy and disposal of waste in the production process, to, finally, the capacity of the product when its life span is ended for recycling or disposal.

In a previous lecture I have already explored the environmental pressures on business, in asking 'How green is your company?', so I shall limit myself here to considering the more specific issue of environmental auditing or what has come to be called 'green accounting'. In particular, how does the environmental audit compare with the earlier stage of social audit and the difficulty of applying cost-benefit analysis to the recognition and weighing of many disparate and variable factors? It appears that the environmental audit is a more manageable exercise than the social audit, and that perhaps for at least two reasons. One is that the field of interest is, at least in principle, narrower and more specific in concentrating on areas of environmental sensitivity rather than on the whole spectrum of social expectations of business. Of course, the field of environmental application is expanding continuously, not only in terms of new products and processes but also in the application of environmental principles to factory and office conditions of work and resources. Even so, concentrating on environmental issues does produce a narrower field of vision than using the wide-angle lens of social responsibility, and so makes the subject a more manageable one to handle and to account for.

The second major difference between environmental auditing and social auditing, which rises from the narrower field of interest, lies in the existence of more recognisable standards of performance and success. Financial considerations still enter into the estimating and assessing of costs to the company, but the idea of quantifying positive benefits to the company in almost entirely financial terms is more readily replaced by the recognition that it is aimed at satisfying a series of external criteria. Again, of course, it can turn out that taking an environmentally-sensitive approach to one's products and services will yield some financially profitable results, and this happy eventuality can be factored into the environmental books. But the major consideration in conducting the environmental audit appears to be one of recognising and taking into account the specific yardsticks of the requirements and expectations which are becoming increasingly expressed by society in this area, whether through legislation at home or in Brussels, or through international conventions, or through subscription to the Valdez Principles, or less formally through mounting public and media pressure.

Ultimately, perhaps, however, for a company the major environmental accounting question may be 'Can we afford not to be environmentally aware?' And to that extent costs arising from introducing changes, or from meeting more exacting standards, or even from paying penalties or fines, will enter into a company's environmental calculations. Such financial auditing can then provide some estimate of some of the costs of being green, or of going green, or even of becoming greener. And within that context the application of criteria of cost-effectiveness can help identify, for instance, the least expensive of several possible energy programmes, or the cheapest source of recycled office paper. But it is still difficult to know just what can be set down in the credit column to offset such costs, other than compliance with accepted standards of behaviour and the literally inestimable consequences of such compliance. It is apparently notoriously difficult to quantify and factor in the brand-value of various products on the market, and *a fortiori* it must be even more difficult to put a price-tag on the environmental status or reputation of a company.

III

A more recent approach to the whole idea of ethics auditing for companies which is being advocated in Britain takes on board the growing concern with environmental issues, but widens the field again to take account of other social consequences of the conduct of business. This is the approach referred to as Corporate Social and Environmental Accounting, or CSR, 'Corporate Social Reporting', in which one of the most influential writers in this country today is Professor R H Gray, Mathew Professor of Accounting and Information Systems in the University of Dundee.

As described by Professor Gray and others, Corporate Social Reporting is 'the process of communicating the social and environmental effects of organisations' economic actions to particular interest groups in society and to society at large'. And as a professional accountant Professor Gray envisages a widening of the accounting process to record and communicate such corporate behaviour in response to growing public expectations concerning the environment and other aspects of life in society.

It will be interesting to note the future prospects of such enlarged accountancy programmes and procedures, particularly in the light of two questions which occur to mind. One is whether accountants are the best profession to undertake such an enlargement of their traditional financial role. And the other, which underlies this, is whether the model of financial auditing and accounting is an appropriate one to be entirely satisfactory for what is envisaged. As may have become clear in the course of my remarks, the move towards companies giving an account of their social activities and impact in financial terms or their equivalent, is bedevilled by the strait-jacket of cost-benefit analysis and by the need to find some basic unit of quantifying and comparability.

Undoubtedly there are financial considerations to be taken into account in all business activities, but as we have seen, while it may be possible to estimate or calculate some of the costs of a company's social activities it is almost impossible to do the same for the other side of the ledger and to assess what benefits may accrue to the company. Moreover, such a company-centred model can only with difficulty take into account the benefits which result for others from enlightened corporate social policies. And there may be the underlying assumption through extending the model of accountancy to a company's social accountability that the ultimate criterion remains the bottom line.

To conclude on a more positive note, however, I want to suggest that more important than how a company's record is calculated and communicated, and by whom, there is a prior and more important stage which might be appropriately called an Annual Company Ethics Review. And that, while this must inevitably include some financial considerations, the weaknesses of the accountancy model which I have mentioned would argue against describing this annual ethics review in terms of an audit. It would in fact be a comprehensive review of all the company's activities during the past year in the light of ethical considerations; and since I have an aversion to what I call 'would-be' writing or speaking, let me describe such a review in terms of what it is, rather than what I envisage it would be.

A designated group of members of the company, including non-executive directors and representatives from all levels of operation, and reporting to the Board of Directors, conducts an annual examination of the company's ethical performance, within the four concentric circles which cover the firm's activities, and which I have described in previous Gresham lectures: starting with the organisation's *internal activities*, including its choice and treatment of employees, the quality of communication, and the recognition of individual rights as well as the responsibilities of the work force, managers and shareholders; then moving out to a second circle of *customer relations*, where what the company produces, as well as its product safety and quality, its advertising and customer satisfaction figure large; moving further to the circle of the company's relations with *other firms*, whether as suppliers or competitors, and examining how fair one's dealings have been with them; and finally considering the fourth and outer circle, the *community* of which the company is an integral part, where the company's impact on not only the physical environment, but also on the social and political environments form the agenda.

The yardsticks or criteria which are applied in the conduct of such a regular company ethics review are several. First and most obviously, the law of the land, certainly in its letter if one is to be law-abiding, but also in its spirit if one is to be ethical. A second set of standards can be industry-wide agreements, or the canons of various professions. Then, importantly, the company's own mission statement, code of conduct, or statement of what it considers best practice; and herein lies the acid test of any corporate statement of ethical standards, that it be observed and applied, that non-compliance be sanctioned realistically, and that it be regularly scrutinised and updated when necessary. A third criterion which the company can apply is its own procedures for internal complaints and whistle-blowing, as well as the mechanisms which it has in place for dealing with customer, public or supplier complaints. And finally, reference can be made to the goals and targets which the company may have set itself, in such areas as environmental respect and affirmative action.

You will note that all the items which I have mentioned have to do with the normal day-to-day activities of the company, and that raises what I consider a most important point about the social responsibility of businesses. In the field of external relations, it is not too difficult for a company to decide on devoting, say a variable proportion of its income to charitable and social activities, and in my last lecture I considered some aspects of this corporate activity of sponsorship. It remains, however, that important and beneficial although what I prefer to call such extra-mural corporate activities are, they cannot ethically substitute for the conduct of business, far less cover up for any ethical shortfall in the run-of-the-mill activities of the firm.

Should such an annual company ethics review be made public, as is becoming required of environmental auditing and expected of social auditing? On the whole, I should say not, since that way lies at least the danger of puffery and lack of candour. This is not to say that an Annual Report may not contain some reference to corporate respect for ethical values. But the purpose of the ethical exercise is more domestic and serious than that.

Ultimately such a review is based on the ethical bedrock which underlies all formal statements of company policy or professional or legal requirements: what may be considered the basic human decencies of fairness, honesty and reliability. If these are approached in auditing or accountancy terms, as I have suggested, they may tend to confuse financial accounting with moral accountability, and obscure the fact that there are some things in the conduct of human beings, including in the conducting of business, which are worth doing for their own sake, whatever the cost. And it is basically these criteria and values which not only give the ultimate *raison d' être* to business, but are sufficiently important to call for regular reconsideration and review of the way in which business is conducted in society.