

What do We Mean by Ethics in Finance?

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1 Dedication

If you were to try to describe the scientific community within the nomenclature of families, then *Albrecht Weber* would have been my brother for more than 40 years. We had with Professor *Hugo J. Hahn*¹ the same *spiritus rector*, who encouraged our interests in International and European Law. We became close friends and neighbours in the Austrian Salzkammergut. During common sailing trips on Lake Mondsee and when we visited the Salzburg Festival we developed a common understanding of approaching legal issues in an international context, which fits well with the title of this *liber amicorum*.

Albrecht Weber – we call him Peter – is a specialist in the field of comparative law. Therefore, I will try to continue my recent work in the context of MOCOMILA² to describe on a comparative basis some developments in the field of ethics in finance, which I assume is undergoing a transformation process from standards of ethics into binding norms.

2 Ethics in Finance?

The international banking crisis that began in 2008 and later developments have once again highlighted the problem that legally permissible behavior need not necessarily be ethical.³ The United States pursued a strategy – allowed by US laws – to

¹ *Hugo J. Hahn* was in 1969 one of the founding members of the Faculty of Law at the Johannes Kepler University in Linz (Austria) and head of the Institute for International Law and International Relations; from 1974 he was full professor and director of the Institute of International Law, European Law and International Economic Law at the University of Würzburg.

² The Committee on International Monetary Law of the International Law Association (www.mocomila.org).

³ Arrigunaga 2000, p. 323 referring to “Deposit Insurance Schemes” (DIS): “DISs erode market discipline. To the extent that depositors and other creditors are protected, DISs reduce their in-

force non-US institutional investors to (partly) restructure some American Banks (e. g. Washington Mutual Inc.).⁴ In the wake of the banking crisis a depletion of trust with negative effects for financial stability occurred.

A first proposal to deal in more detail with questions of ethics in finance came from *William Blair*, the Chairman of MOCOMILA, when he prepared the agenda for the MOCOMILA-Meeting in Madrid (September 2013). He stated in his remark “Is there a role for culture and ethics in financial regulation?”⁵ that it is not always easy to pin down in the highly competitive commercial environment of international finance “what conduct is ethical”. This question includes first the assumption that there is already a consensus concerning the vital role of ethics in finance and involves secondly doubts about whether ethics in finance is a “subset of general ethics”.⁶

Some authors have argued that in the field of finance there is no ethics. Or in other words: “Finance and [...] ethics [...] do not belong together.”⁷ In fact, the recent financial crises may lead to the conclusion of a “disconnect between ethics and finance”⁸ or – with view on the *Ponzi* scheme conceived by *Bernard Madoff* – “of a real divorce of ethics from finance”.⁹ But the concept of “divorce” contains the statement that ethics and finance were once “married”. *Fernandéz* cites – referring to *Ferullo*¹⁰ – “three stages in the modern history of economic thought: first, where finance and ethics were united; second, where they were rubbing shoulders; and third, where the separation was complete”. But no one could be found who would have been happy with this development. And no one could be found who would not have argued for the importance of ethics in the field of finance. Overall, it may be assumed that there is a broad consensus that finance should not be conceivable without ethics.¹¹

The second question concerns the very core of this topic: Is there a special ethics for the field of finance and if so, how many?¹² Reflecting the large number of existing different “codes of ethics” or “codes of conduct”¹³ one might get – at a first glance – the impression that market participants tailor in a kind of do-it-yourself method their own specification of ethics in finance. Consequently, *William Blair* argues that “[f]urther analysis of the codes could usefully be done to identify what is

centive to monitor the financial condition and risk policies of banks. This behaviour allows bank owners and managers to engage in high-risk projects without having to pay a cost for doing so.”.

⁴ Zehetner 2009.

⁵ Blair 2013, p. 10.

⁶ Sifah 2012, p. 155.

⁷ Ranaivoson 2012, p. 191.

⁸ Fernandéz 2012, p. 297.

⁹ Fernandéz 2012, p. 298.

¹⁰ Ferullo 2010.

¹¹ Blair et al. 2014.

¹² This wording refers to the German title of the philosophy published 2007 by *Richard David Precht*: “Wer bin ich – und wenn ja wie viele?” (“Who I am – and if so how many”).

¹³ See the list prepared by Blair 2013, p. 8 and those ethical codes and codes of good conduct described by Sifah 2012, p. 159.

common ground, and where the differences are”.¹⁴ The notion of “difference” raises the further question whether codes of ethics in finance cannot only be different, but can also be in contradiction to each other. It must be assumed that a substantive difference in codes of ethics would – by definition – be *unethical*. But what could be used as a global benchmark for the ultimate decision on what is ethical and what is unethical in finance?

3 Global/General Ethics

On 4 September 1993 the Parliament of the World’s Religions endorsed in Chicago a “Declaration Toward a Global Ethic”.¹⁵ The basic approach of this conference was to determine the common ethical principles of the world’s religions and to publish these principles in many languages. This conference confirmed “that there is already a consensus among the religions which can be the basis for a global ethic – a minimal fundamental consensus concerning binding *values*, irrevocable *standards* and *fundamental moral attitudes*.” The basic principle (in the German version: “the golden rule”) which should be the irrevocable and unconditional norm for *all* areas of life, has the following wording: “What you do not wish done to yourself, do not do to others.” This principle is also formulated in positive terms: “What you wish done to yourself, do to others!” This basic principle seems from the point of view of consequences very similar to *Kant’s* “Categorical Imperative”: “Act only in accordance with that maxim through which you can at the same time will that it should become a universal law without contradiction.”¹⁶ These similarities led to the widespread view that these two principles are identical.

4 Ethics in Finance!

In order to prevent misunderstandings, it should be pointed out that it is not the intention of this contribution to distinguish between global ethics and ethics in finance. On the contrary: Ethics is not divisible, but you can distinguish different *layers* of ethics. In fact, some principles of ethics play a more important role in finance than in other areas of life. In this context, reference may be made again to the “Declaration Toward a Global Ethic”, as mentioned above. Part III (“Irrevocable directives”) subtitle 2 (“Commitment to a culture of solidarity and a just economic order”) contains a directive, which was found by the Parliament of the World’s Religions in “the great ancient religions and ethical traditions of human kind”: “You shall not steal” or (in positive terms) “Deal honestly and fairly”. The

¹⁴ Blair 2013 p. 10.

¹⁵ Cf. Global Ethic Foundation at http://www.weltethos.org/1-pdf/10-stiftung/declaration/declaration_english.pdf. Accessed 28 August 2013.

¹⁶ Kant 1786/1993.

Parliament clarified this directive that “no one has the right to use her or his possessions without concern for the needs of society and Earth”. This example shows that this clarification in the Declaration is only a lower layer of the basic principle of global/general ethics, the golden Rule or *Kant*’s “Categorical Imperative”. The ethical directive “You shall not steal” is therefore only the more comprehensible expression of the basic principle of global/general ethics and there is also no contradiction.

Having this in mind you can start to analyze the existing “codes of ethics” or “codes of conduct” as further layers in this *holistic* approach to ethics: Look, for example, into the decision tree of the Code of Conduct of JPMorgan Chase & Co¹⁷ with the questions “Would it be okay if everyone did it?” and “Am I sure I would not feel uncomfortable or embarrassed if I read about it on the front page of the newspaper?”.¹⁸ If you go into a more detailed analysis of the substantial rules of these codes, then you will find the above-mentioned basic principle of ethics but formulated in a more operative manner: The above-mentioned ethic directive “You shall not steal” (which is already a clarification of the basic principle “What you do not wish done to yourself, do not do to others”) was translated in the Code of Conduct of JPMorgan with a short question and a clear answer: Q: “A co-worker asks me to share marketing strategies we used at my former company. Can I do that?” A: “You must not disclose that information. The marketing strategies of your former employer are likely to be proprietary and you have the obligation to protect them, even after leaving that company. Remember, you will have an obligation to protect the proprietary and confidential information of our Company, too, should you leave to work somewhere else.” This seems to be an excellent example to show that ethics is indivisible and that the different aspects of ethics only reflect the basic principles of ethics.

We can summarize as an intermediate result: Ethics in finance means the specification of the general principles of ethics for the purpose of application and compliance in the field of finance. “Codes of ethics” or “codes of conduct” are only instruments to specify these general principles for this purpose, provided that they are consistent with the general principles of ethics.¹⁹

5 Ethics and Law

In describing the interactions between ethics and law even the lawyers have learned their lessons: *Bill Blair* explained us – referring to ethics in finance – that “it has to

¹⁷ JPMorgan Chase & Co., Code of Conduct, June 2013, http://www.jpmorganchase.com/corporate/About-JPMC/document/229048_2013_CodeofConduct_05.31.13_ada.pdf

¹⁸ JPMorgan Chase & Co., Code of Conduct, p. 4.

¹⁹ Blair et al. 2014 p. 5: “Codes of conduct can play an important role in maintaining ethical standards if they are treated as part of the operation of the business. They can also contain a useful expression by those who actually run financial institutions of what they regard as ethical conduct.”.

be recognized that there are the limits as to what further regulation can achieve”.²⁰ And *John Plender*, a senior editorial writer and columnist at the Financial Times wrote that “[w]e have learned from experience that it is not possible to regulate people into good behaviour”.²¹ Although these observations seem to be correct, they reflect a certain contradiction with the legal reality: The extensive practice of “codes of ethics” or “codes of conduct”, not only to define rules of ethics but to connect non-compliance with legal consequences, irritates. Are the rules of ethics (as defined in these “codes”) changing their quality and are they becoming “binding rules”?

The following comparative analysis of some codes should provide a basic understanding of the phenomenon of transferring ethics into binding rules:

First, it should be emphasized that the terms “code of ethics” and “code of conduct” are merely descriptive, not normative. This means that with the use of these terms no information on their legal quality and their binding effects is connected. For this reason, many *definitions* of “code of ethics” contain – at a first glance – no express guidance relating to their possible binding effects:

“A guide of principles designed to help professionals conduct business honestly and with integrity. A code of ethics document may outline the mission and values of the business or organization, how professionals are supposed to approach problems, the ethical principles based on the organization’s core values and their standards to which professionals will be held.”²²

“A written set of guidelines issued by an organization for its workers and management to help them to conduct their actions in accordance with its primary values and ethical standards.”²³

“A code of ethics is a formal document rather than merely an ‘environment’, an ‘understanding’, a ‘consensus’, ‘unwritten rule’, or just an aspect of ‘corporate culture’. It is at minimum a published document.”²⁴ “Codes of ethics are free-standing expressions of corporate will even when they are published as chapters or sections in a document which may contain a mission statement, a listing of corporate values, and general policies relating to operations.”²⁵

“Codes of ethics codify the values and principles of the company and define the responsibilities, duties and obligations organizational members have to the organization and its stakeholders.”²⁶

²⁰ Blair 2013, p. 4.

²¹ Plender 2012, p. 16.

²² Investopedia, Code of Ethics, <http://www.investopedia.com/terms/c/code-of-ethics.asp>. Accessed 22 December 2014.

²³ BusinessDictionary, Code of Ethics, <http://www.businessdictionary.com/definition/code-of-ethics.html>. Accessed 16 October 2014.

²⁴ Inc., Code of Ethics, <http://www.inc.com/encyclopedia/code-of-ethics.html>. Accessed 24 September 2014.

²⁵ Inc., Code of Ethics.

²⁶ Educational Portal, Code of Business Conduct: Ethics, Standards & Examples, <http://education-portal.com/academy/lesson/code-of-business-conduct-ethics-standards-examples.html>. Accessed 27 February 2015.

The finding that a code of ethics is – by definition – not necessarily binding must not be misunderstood to imply that it cannot be binding. On the contrary: Some argue, that “a code of ethics without sanctions [. . .] will be viewed by employees as merely a gesture without ‘teeth’”.²⁷ Consequently, it is postulated that a “properly framed code is, in effect, a form of legislation within the company binding on its employees, with specific sanctions for violation of the code”.²⁸

A detailed analysis of numerous codes of ethics shows that in many codes of ethics their binding effect is established by the code of ethics itself. Each norm addressee falling within the personal scope of the code has the obligation to comply with the code:

“Bank of America Corporation is committed to the highest standards of ethical and professional conduct. To help you understand how these standards apply to you and your teammates, this Code of Ethics provides basic guidelines for our daily conduct you are expected to adopt and uphold as a Bank of America *associate*.”²⁹ The term “associate” is defined in a footnote and refers “to any Bank of America director, officer or employee”.³⁰ These “associates” are the norm addressees of this code of ethics. The obligation to comply with this code of ethics is expressed with the “soft” wording that associates “are *expected* to follow the information in this code”.³¹ However, to avoid misunderstandings that this could be only a recommendation, the introduction to this Code of Ethics ends with a reference to the legal consequences of violations of this Code: “Violation of the Code of Ethics or these other policies, law or regulations constitutes grounds for disciplinary action, including termination of employment and possible legal action.”³² All substantive elements of a binding rule are given and all ethical principles, as defined in this Code of Ethics have become binding for the associates (as norm addressees).

A very short (two pages) Code of Ethics was published by the CFA Institute:³³ The enumeration of six principles of ethics is preceded by an introduction that firstly describes the norm addressees and secondly establishes the liability: “Members of CFA Institute (including CFA charterholders) and candidates for the CFA designation (‘Members and Candidates’) must: [. . .]”.

The “sanctions” are described in the “Preamble”: “Violations may result in disciplinary sanctions by CFA Institute. Sanctions can include revocation of membership, revocation of candidacy in the CFA Program, and revocation of the right to use the CFA designation.” Again, all substantive elements of a binding rule are given.

²⁷ Inc., Code of Ethics.

²⁸ Inc., Code of Ethics.

²⁹ Bank of America Corporation, Code of Ethics, revised January 2009, http://www.media.corporate-ir.net/media_files/irol/71/71595/corpgov/CodeofEthics12908.pdf. Accessed 22 November 2014. p. 5 (emphasis added).

³⁰ Bank of America Corporation, Code of Ethics, revised January 2009, p. 6 footnote 3.

³¹ Bank of America Corporation, Code of Ethics, revised January 2009, p. 6 (emphasis added).

³² Bank of America Corporation, Code of Ethics, revised January 2009, p. 6.

³³ CFA Institute, Code of Ethics and Standards of Professional Conduct, <http://www.cfapubs.org/doi/pdf/10.2469/ccb.v2014.n6.1>. Accessed 15 September 2014.

The “Code of Ethics and Business Conduct” of U.S. Bank³⁴ contains all substantive elements of a binding rule in a blue coloured frame, which is part of the table of contents:³⁵ It is worth mentioning that this section starts with the sanctions: “*Anyone* who violates the U.S. Bank Code of Ethics and Business Conduct may face disciplinary action, up to and including termination.”³⁶ But the term “anyone” is restricted in the very next sentence to the effect that the “U.S. Bank Code of Ethics and Business Conduct applies to all employees and directors of U.S. Bank and its affiliates”. Again, all substantive elements of a binding rule are given.

The “Code of Business Conduct and Ethics of UBS”³⁷ contains two of the substantive elements of a binding norm in its “Preface” (concerning norm addressees and binding effects): According to the first paragraph of the preface this code “sets out the principles and practices that are *binding for all of the UBS’s employees and Board members* to follow unreservedly both in letter and in spirit”.³⁸ In the last paragraph of the preface, the binding nature of the UBS-Code is emphasized again: “Compliance with the principles set out in the Code is mandatory.”

The chapter “Disciplinary measures”³⁹ contains the two subchapters “Violations” and “Appropriate action”. In subchapter “Violations” is twice – that is redundant – very strikingly expressed that UBS will not tolerate violations of the Code. Subchapter “Appropriate action” refers to the appropriate actions of UBS to address violations: “Disciplinary measures may include reprimands, warnings, demotion and dismissal.” Again, all substantive elements of a binding rule are given.

The substantive elements of a binding norm are formulated very clearly also in the RZB Group Code of Conduct (“RZB Group CoC”):⁴⁰

The norm addressees, called “Target Group”, are defined in Sect. 1.2 § 1 RZB Group CoC as follows: “The provisions of the RZB Group CoC apply to, and have to be observed by, all employees of the RZB Group globally.” Section 1.2 § 2 RZB Group CoC refers to some details concerning the question of what is really meant by “globally”: “Thus the RZB Group CoC applies to all employees in foreign branches, subsidiaries, whether directly or indirectly controlled by RZB, and companies in which a majority interest is held.” Very interesting is the last sentence of Sect. 1.1 § 2 RZB Group CoC, which takes into account the fact that the RZB Group CoC cannot be binding on third parties without further act: “In addition, all third parties acting on behalf and/or in the name of RZB Group must commit themselves to comply with the provisions of the RZB Group CoC.”

³⁴ US Bank, Code of Ethics and Business Conduct. Integrity * Respect * Responsibility* Good Citizenship, <https://www.usbank.com/hr/docs/policies/coeHandbook.pdf>. Accessed 5 December 2014.

³⁵ US Bank, Code of Ethics and Business Conduct, p. 4.

³⁶ Emphasis added.

³⁷ UBS, Code of Business Conduct and Ethics, download from https://www.ubs.com/global/en/about_ubs/about_us/code_of_conduct.html. Accessed 12 October 2014.

³⁸ Emphasis added.

³⁹ UBS-Code, p. 10.

⁴⁰ RZB group, Code of Conduct, http://www.rbinternational.com/eBusiness/services/resources/media/829189266947841370-829188968716049154_866477530159365956-829819009011584386-1-2-EN.pdf. Accessed 28 November 2014.

Furthermore, it is made perfectly clear in Sect. 1.3 § 1 RZB Group CoC that this Code is *binding*: “The RZB Group CoC is a binding set of rules governing everyday business dealings. The pursuit of profit does not justify any breaches of the law or the RZB Group CoC.” This results in a *de facto* equality of the RZB Group CoC with the laws.

Finally, the RZB Group CoC also contains “Sanctions in Case of Violations of the RZB Group CoC”:⁴¹ “The RZB Group CoC forms an integral part of the general conditions of employment. Therefore, any breach of the RZB Group CoC has consequences under labour law and can be sanctioned by disciplinary measures, including termination of the employment without notice.” Again, all substantive elements of a binding rule are given.

We can summarize as a further intermediate result: The codes of ethics as outlined above have in common that they *are* binding rules. The rules of ethics (as defined in these “codes”) have changed their quality and become “binding rules”. This also means that these specifications of general ethics have to be interpreted using the legal interpretation methods. The principles of general/global ethics (as mentioned above) will play an important role in the teleological interpretation of the individual codes of ethics.

From the viewpoint of their substance, the codes of ethics generally (i. e. not only in the field of finance) differ significantly: There are very short codes of ethics referring only to the principles of general/global ethics and there are also very extensive codes of ethics with very detailed and differentiated specifications of ethics, specially designed for the area in which the relevant company operates.

Furthermore, it was noticed that the title of the code (“of ethics”, “of conduct” or “of ethics and conduct”) refers to the main focus of the individual code: Codes of ethics focus on ethics and codes of conduct focus on conduct. Codes of conduct very often relate also to issues for which one cannot at first sight see the connection with the subject of ethics:

Take for example the RZB Group CoC, which also rules that the “RZB Group does not participate in the construction of nuclear power plants nor does it do business with nuclear power plants or their operators”. This – binding – rule was therefore supplemented by an “ethical” reason: “Recent experiences show that the risks, associated with nuclear power plants both to the environment and human beings are currently not manageable.”⁴² The ethical justification of the rule concerning non-participation in business connected to war material weapons and other military equipment⁴³ is not apparent at first sight but can be found in the *argumentum e contrario*: “RZB Group does not participate in business connected to war material weapons and other military equipment (including equipment used for internal repression or aggression against foreign countries) with countries having ongoing or expected military conflicts or political unrest”. *Argumentum e contrario*: Business connected to war material weapons with countries *not* having ongoing or expected

⁴¹ Section 1.8 RZB Group CoC.

⁴² Section 7.3 RZB Group CoC.

⁴³ Section 7.4 RZB Group CoC.

military conflicts or political unrest is *not* covered by this rule and seems therefore to be “ethical”. Or not?

In any case, these two examples of a well-designed code of conduct show that the limits of what is ethical and what is not ethical seem very vague. It is therefore necessary to point out the duality of the global/general ethics to their specifications in the various codes of ethics in the field of finance. The latter *specify in binding form* the principles of global/general ethics, without thereby relieving the addressees of their moral obligation to comply with the principles of global/general ethics. “Even if the provisions of codes are followed to the letter, the ethical spirit which they are intended to embody may still not fully become part of a bank’s culture in practice.”⁴⁴

6 Conclusions

- Ethics in finance means the specification of the general principles of ethics for the purpose of application and compliance in the field of finance.
- “Codes of ethics” or “codes of conduct” are instruments to specify these general principles of ethics for purposes of practical application.
- The majority of “codes of ethics” and “codes of conduct” are binding for the addressees listed in the relevant code.
- The majority of “codes of ethics” and “codes of conduct” contain sanctions.
- The rules of ethics (as defined in these “codes of ethics”) have changed their quality and became “binding rules”. These specifications of general ethics have to be interpreted using the legal interpretation methods. The principles of global/general ethics (as mentioned above) will play an important role in the teleological interpretation of the individual codes of ethics.
- “Codes of ethics” and “codes of conduct” do not relieve their addressees of their moral obligation to comply with the principles of global/general ethics.

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⁴⁴ Blair et al. 2014, p. 5.

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