

# Corporate Integrity

## Just a Concept or Real Behavior/Practice

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### Introduction

**T**HE ECONOMIC crisis of 2008 brought with it, in addition to all the unethical behavior, a chance to reflect on good corporate governance and management. The legal and ethical scandals of Enron, WorldCom, Tico and many other companies initiated a wave of mistrust. After discussions about how to emerge from the occurred situations, various initiatives for doing business on different foundations have been undertaken. It is not surprising that the business world has realized that a new era of corporate governance and management must begin. Companies' governance and management processes must be much more grounded on the implementation of business ethics, the review and monitoring of corporate strategy implementation and the evaluation of board performance. The principles of corporate integrity have become an essential part of corporate governance and management today. Companies with a high level of corporate integrity have become more successful, showing better business results (see Belak Ja. et al., 2014; Bleicher, 1994; Rüeg-Stürm, 2002; Widana et al., 2015; Ferrel et al., 2011; Hassan et al., 2008). The fiasco in September 2015 of one of the world's automotive giants, VW Group, on the United States market, clearly shows the consequences of fraudulent, irresponsible and unethical conduct.

We recognize the importance of corporate integrity as an appropriate tool for the efficient guidance of companies, which unites all relevant, internal, and external stakeholders. Therefore, we decided to explore corporate integrity by applying the principles of the Organization for Economic Co-operation and Development (OECD; Towards a Sound Integrity Framework: Instruments, Processes, Structures and Conditions for Implementation, 2008) and Maak's (2008) framework to seven aspects of corporate integrity, called the "7Cs," in relation to the MER model of integral management (Belak Ja. et al., 2014) and considering the levels of business ethics (Thommen, 2003).

The main motivations for our research were twofold: first, a real event (i.e. our case study), which happened to one of the researchers, and second, the guidelines on corporate integrity that were adopted in Slovenia almost at the same time as the event/case under investigation.

The main purpose of our research was to explore the theoretically developed concept of corporate integrity and the OECD principles in a real-life situation in order to

deepen our understanding of how the concept works in practice. In our opinion, corporate integrity should be approached in a holistic manner. Therefore, we incorporated the concept of corporate integrity as well as the OECD principles in the MER model of integral management and governance (Belak Ja. et al., 2014). Since the examined and studied case (company) shows bad corporate integrity practices, the main research question in our study is: How should the concept of corporate integrity be transformed into a more reliable system in practice?

The elements presented in this paper can be useful in developing a theory of corporate integrity. The findings derive from an in-depth case study of a construction company in Slovenia where the negative experience of a customer called into question the corporate integrity of that company. A single-case study has been conducted that enables an “analytical generalization” in which “a previously developed theory is used as a template with which to compare the empirical results of the case study” (Yin, 2003, pp. 32-33). By comparing the principles of both mentioned concepts and the findings of the case study, we believe that imperfections in the corporate integrity concept can be recognized. Therefore, our contribution to the theory of corporate integrity is the identification of weaknesses in corporate integrity and the discussion of how to improve corporate integrity in order to make it more efficient.

The paper is structured as follows. We start with the theoretical framework of the concept of corporate integrity, focused on the OECD’s principles and Maak’s “7Cs” framework of corporate integrity. We illustrate the Slovenian guidelines of corporate integrity, which have been adopted by 29 identifiable Slovenian companies to date. The main research work is concentrated on the case study, which refers to the contractual relationship between a company and a customer, with a legal analysis of the observed relationship and its assessment of conformity with ethical principles. Furthermore, we place the above-stated principles and Maak’s “7Cs” of corporate integrity into the MER model of integral management as the argument for the companies’ successful integrity implementation.

## 2. Theoretical Framework

### 2.1. The Concept of Corporate Integrity

**C**REATING A concept of corporate integrity has been a long-term process which started in the early 1950s. One of the first authors to deal with the social responsibility of businesses was Frank Abrams, Standard Oil’s executive director. By publishing his article, “Management’s Responsibilities in [a] Complex World,” in the *Harvard Business Review* in 1951 he created an awareness of corporate integrity through the domains of social responsibility and corporate social responsibility. He tried to influence his fellow managers’ speculations about their status in society and, in particular, their responsibility to society, not only in the context of individual responsibility to shareholders but in the broadest sense of their responsibility to the public in general (Maak, 2008, p. 354).

In the 1970s, serious efforts to define corporate social responsibility, including notions like legal responsibility of a corporation, a corporation’s charitable action, being ethical, and ensuring legitimacy (Eels & Walton, 1974), began to emerge.

In the 1980s, the discussion of corporate social responsibility (CSR) tried to define the moral status of corporations, while the 1990s brought specialization into business ethics theories and attention to issues involving global business ethics. After the Enron scandal, CSR became an instrument to benefit the corporation and was transformed from CSR to strategic social responsibility (SCR). The new perspective sees CSR as a (strategic) response to changing circumstances and new corporate challenges. Organizations must rethink their position and act in terms of the complex societal context of which they are a part (Marrewijk, 2003, p. 97).

Today, CSR is faced with different challenges, social, moral, environmental and humanitarian. These diverse areas by inference affect several research domains which are connected by the same purpose: dealing with ethical issues in business. They all should be connected and discovered under some kind of integration work, called “corporate integrity,” as an umbrella term (Maak & Ibid., 2008, p. 357).

## 2.2 Definition of Integrity and Corporate Integrity

INTEGRITY IS defined as “the state or quality of being entire or complete: wholeness; entireness; unbroken state and moral soundness: honesty; freedom from corrupting influence or motive” (see *Webster’s Dictionary*, 1913; Maak, 2008). Both meanings complement one another and indicate that integrity involves an undivided, completed whole, acting in accordance with moral principles like honesty, sincerity, and confidentiality. Moral integrity starts with the commitment to comply with moral principles and continues with moral conduct to fulfil integrity requirements on environmental, ethical, political and social fields.

In Latin, integrity means “not touching” (in tangere) and defines something or someone who is not contaminated. In the context of creating an integrity framework, it means the application of generally adopted norms and values in daily practice (OECD, 2009, p. 9). However, to achieve integrity, core elements have to be involved:

- The integrity management instruments, which constitute the integrity management system by defining integrity (codes of conduct or codes of ethics), by managing integrity, supervising compliance and enforcing integrity (the integrity management framework).
- The instruments of the integrity context, which include factors outside and inside the organization other than the instruments of the integrity management system (OECD, 2009, pp. 9, 33).

To achieve a holistic view of corporate integrity, the “wholeness” of the corporation, we specify five levels of corporate integrity: interpersonal, organizational, cultural, social and natural. Each is important for assessing the integrity of a corporation and also for improving it. On the interpersonal level of corporate integrity, the focus is on relational awareness. Communication between workers and managers is needed because workers are not involved only in relationships at work, but also have relationships with families and the civil society. The cultural level indicates that corporations must be open to other cultures and directed by worthwhile purposes (organizational level). Social challenge is concentrated on the development of relationships with other private and government agencies. Corporations have to address the natural environment to provide prosperity for all natural communities (Brown, 2006, p. 15).

Individuals possess integrity if they follow moral principles and act honestly, credibly, loyally and trustworthily, even when they have to abandon self-interest to act in line with moral values. In contrast, the integrity of an organization (including a corporation) applies not only to its members but also to its structure, function and culture. It is mostly concerned with the integrity of its members, their individual integrity, but also with essential differences; in the case of corporate integrity, individual integrity depends on the constitutive virtues of the individual role in terms of professional responsibility (O'Brian, 2007, p. 355).

In discussing integrity systems at the macro-institutional level (for more about levels of ethical relationships, see p. 12, subchapter 3.4.2), Miller (2007) established that regulatory frameworks and integrity systems do not represent identical notions. A regulatory framework consists of a set of definite laws, rules or regulations governing behavior and minimum ethical standards, usually incorporated in a law passed by an institutional authority, with provided sanctions. The integrity system is a train of institutional entities, roles, mechanisms and procedures, whose purpose is to ensure compliance with minimum ethical standards and promote the pursuit of ethical goals, while calculation on law is generally missing (Miller, 2007, p. 354).

Maak (2008) created an interesting theoretical framework based on seven distinct aspects, commitment, conduct, coherence, content, context, consistency and continuity (the "7 Cs") of corporate integrity, which must be connected in a cycle of relational wholeness to become an "undivided corporate self" (p. 365).

Integrity behavior does not concern only closer persons (shareholders) but all relevant others. Integrity demands coherence between commitment and conduct, meaning that the corporation has to do as it promises. The right context demands regular relationships, both close and distant. The right content means doing the right thing and acting responsibly. Continuity demands that the corporation or the person (Maak illustrated the case with a whistleblower, p. 359) act in accordance with integrity requirements for years in order to prove integrity. Consistency means being honest and sincere about the corporation's CSR achievements and its failures; CSR reports should not be just a "selling device" but an instrument for authentic representation and stakeholder dialogue.

Therefore, we can state that the wholeness (holism) of a corporation is structured from different integrity levels. First, individual integrity includes all individuals, executives and employees. Second, corporate integrity represents the level of the organization and, third, stakeholder integrity consists of all individuals or groups that have a legitimate interest in, are affected by or could be affected by the activities of both the corporation and its members. The above-stated integrity levels may conflict with each other. However, note that to reach a level of corporate integrity, all participants (individuals, the corporation and other stakeholders) must resolve conflicts of interest and win this challenge of wholeness (e.g. Kolb, 1988, p. 70).

## 3. Case Study

### 3.1 Research Method

**T**HE IMPETUS for this study was provided by a unique opportunity. The researcher experienced considerable problems with the builder of the researcher's house. The researcher approached her colleagues at the faculty where she works. At first, the researcher looked only for legal advice, but later discussions with other colleagues led to identification of several issues within the problem. During the process of extensive communications with the construction firm (i.e. Company X), the Slovenian guidelines of corporate integrity were signed in Slovenia (discussed in the next section). As a scholar, the researcher recognized that the problem would be an excellent opportunity to study how the concept of corporate integrity works in practice. With this in mind, the researcher established a research team consisting of her colleagues at the faculty. Each team member is an expert in a different scientific discipline (e.g. law, ethics, qualitative research methodology) that has been recognized as important in a holistic approach to the problem identified. The members of the team are at the same time the authors of this contribution.

A qualitative research method was the most suitable approach since social and cultural aspects of organizations are studied (Myers, 2013). Qualitative research is the best way to study a particular subject in-depth "... when the particular topic is new and there is not much previously published research on that topic" (Myers, 2013, p. 9). We decided to use the case study research methodology that has been widely accepted in business and management research (e.g. Eisenhardt, 1989; Myers, 2013; Reay, 2014; Yin, 2003). An important part of a case study design is the selection of a specific type of case study (e.g. Yin, 2003). Since we found our case to be an extreme case showing that corporate integrity is a relevant phenomenon, we decided to apply a single descriptive case study (e.g. De Masis & Kotlar, 2014; Yin, 2003).

### 3.2. Corporate Integrity in Slovenia

EFFORTS TO implement the principles of corporate integrity are also being made in Slovenia. They reached a pinnacle in January 2014, when on the basis of cooperation between the Chamber of Commerce of Slovenia, the Managers' Association of Slovenia, the Slovenian Directors' Association and the Economic Faculty of the University of Ljubljana, under the honorary patronage of the president of the Republic of Slovenia, Mr. Borut Pahor, the Slovenian guidelines of corporate integrity (SSKI) were issued. The purpose was to offer companies in Slovenia an opportunity to systematically exercise the principles of corporate integrity in their business. The formulation of the Slovenian guidelines derived from codes of conduct and Slovenian and international regulations on corporate integrity, particularly emphasized in the OECD Good Practice Guidance on Internal Controls, Ethics and Compliance (2009). By signing the Slovenian guidelines in public, to date 29 presidents of boards, members of boards or directors—the ambassadors of corporate integrity—have committed that their companies will respect and follow the principles incorporated into the Slovenian guidelines on corporate integrity.

SSKI defines “corporate integrity” in the most general and broadest way as the compliance of business companies. Business companies will be in compliance only when their operations are consistent with the legislation, other rules, current recommendations, internal regulations, good business practices and ethical principles (SSKI, 2014, p. 2).

### **3.3. Data Collection and Analysis**

DIFFERENT TECHNIQUES can be applied for data collection within the case study (e.g. Creswell, 2013; Myers, 2013). Interviews and analysis of written documents were assessed as the most appropriate techniques for our case study. Data collection started with an in-depth interview with the researcher, the owner of the house (hereinafter referred to as the customer), which explained the issue under investigation.

In 2003, the customer signed a contract with Company X to build a prefabricated house as an extension of an existing house. In May 2014, the customer discovered that the shingles on the roof of the prefabricated house were considerably damaged. The customer contacted the supplier of the shingles (Company Y) inquiring how it was possible that the shingles had become so damaged in just 11 years. A representative of Company Y came to the customer’s property in May 2014 and examined the roof. He wrote a report on the results of his examination. The major finding of his examination was that the shingles on the roof of the customer’s house were not those that were agreed upon in the contract and paid for by the customer. The customer decided to request replacement of the shingles. The customer sent the request to Company X. The person responsible at Company X’s department for claims responded shortly in a formal letter stating that all terms for the claim had expired. The customer was not satisfied with this answer and proposed a meeting with the responsible persons at Company X. On the date of the meeting, the customer received a phone call from the person responsible at Company X’s department for claims explaining that the responsible person did not have time to meet and saw no reason to discuss the issue with the customer.

Several interviews were conducted with the customer after this initial in-depth interview to collect additional information. In addition to the interviews, we gathered and studied written documents such as the contract between the customer and Company X and written documentation on the communication between the customer and Company X. Data were also collected from Company X’s websites, newspaper clippings and articles appearing in the mass media. The triangulation of data using multiple sources of data (i.e. interview data, documentation) is, in the opinion of several authors (e.g. Creswell, 2013; Myers, 2013), a suitable way to gain a more comprehensive picture of the researched phenomenon and to enhance data credibility (e.g. De Masis & Kotlar, 2014). The interviews and the data collection were completed between September 2014 and February 2015.

Data collection and analysis were guided by the research question and were performed several times concurrently, which is often the case in qualitative research (e.g. Creswell, 2013). When analyzing the case, we used a theoretical framework created on the basis of the existing literature, where two major areas of investigation have been identified: legal interpretation and ethical interpretation. In the next section, we present the findings of the legal and ethical analysis of our case study.

### 3.4. Findings

#### 3.4.1. Legal Analysis

IT IS apparent from the description of the facts that a construction contract concerning an extension to a residential house was signed between the company (i.e. Company X, the contractor) and the client (i.e. the customer). The construction contract was executed with both parties fulfilling the obligations undertaken. Eleven years after completion of the work, however, it became apparent that the contractor had failed to fulfil the contractual obligations by installing a different roof covering, without previously notifying or reaching an agreement with the client. The client was informed of this fact when after barely 11 years the roof covering was destroyed to the extent that it had to be replaced.

The improper performance of the contract described above may be defined as construction with a defect. The contractor's liability for material defects is a contractual obligation according to which the contractor, who constructed a building with defects, is obliged to eliminate the negative effects of such defects and the client has the right to require the elimination of the negative effects. The client exercises this right through an action to enforce a guarantee and through compensation claims.

#### *Civil tort*

In the present case, the contractor's liability for the defect may be founded on two legal bases:

- As general liability for defects in a structure (Art. 633– 640 of the Code of Obligations - OZ).
- As a special type of liability for defects in the execution of the structure concerning its solidity (Art. 662 of the OZ).

It is possible to speak of a defect in a structure when the properties of a built structure fail to comply with the contractually agreed properties and the rules of the construction profession, as it follows by analogy from paragraph 1 of Article 626 of the OZ. It is apparent from the general rules concerning the liabilities for material defects that a contractor is responsible for both the material and legal defects of a structure. In the present case, material defects appeared in the building and, therefore, a discussion of legal defects is not included in this paper.

Special rules on liability concerning the solidity of the structure do not apply to all defects in a structure (unlike the general liability for defects in a structure) but only to defects in parts of the structure allowing its normal use. Other than the defects in the construction parts of the structure, jeopardizing its stability, the defects concerning the solidity of construction also include other defects due to which the stability of the structure is not at risk, but they prevent or substantially hamper the normal functioning of the structure (e.g. defects on the roof or façade causing rainwater penetration into the structure) (Plavšak, 2004).

The contractors' behavior may also be defined as a liability for damages or, more specifically, contractual liability, considering that due to the contractor's breach of contractual obligation the client suffered damage, resulting in a reduced value of the structure with a defect. Given that the liability for defects is a special type of contractual liability for

damages, the relevant claims are already covered by the claims related to the contractor's liability for defects.

### *Criminal offence*

The contractor's behavior may also be defined as business fraud in accordance with Art. 228 of the Criminal Code (KZ-1).

Pursuant to Art. 228 of the KZ-1, business fraud is a special type of fraud that can only be committed in the performance of an economic activity. A perpetrator of this criminal offence does not necessarily have a fraudulent intent from the beginning; performance of such an act is also possible during its implementation. The perpetrator performs a fraudulent act by deceiving the other person (resulting in misrepresentation of specific circumstances to the other person) or leaving the other person in the wrong as regards the existence or non-existence of specific circumstances. A criminal offence is completed when a party or anyone else incurs pecuniary loss (unlawful consequence). The occurrence of the damage must always be conditional upon the act of the perpetrator, which means that a causal link must be established between the perpetrator's fraudulent practice and the occurrence of the damage (Judgment of the Supreme Court of Slovenia, No. I Ips 361/2004 of 2 June 2005).

The legally protected value in this criminal offence is economic activity, whereas the legally protected good is the principle of trust in legal transactions (Selinšek, 2006).

Behavior refers to active behavior, creating misrepresentation by the other party, or passive behavior, leaving the other party in the wrong, and it has to be complemented by obtaining material benefit or by the occurrence of material loss for the party or for anybody else.

The perpetrator commits an act with direct or possible intent, which must be present when concluding or implementing a contract.

Business fraud is punishable by a prison sentence of up to 5 years and from 1 to 10 years for a qualified form of offence if substantial material loss has occurred. Pursuant to the KZ-1, substantial material loss refers to a loss exceeding EUR 50,000 (Art. 99/9 of the KZ-1).

### **3.4.2. Ethical Analysis**

IN THIS article, we examine the ethics and integrity of the observed company at all three levels of ethical relationships: individual, organizational and social (Staffelbach, 1994; Weiss, 2006). Thommen (2003) named these levels the micro, mezzo and macro levels. According to both studies, business ethics is carried out at the organizational (mezzo) level. At all levels, the ethical behavior of a company and its integrity can be fostered and achieved by applying informal measures (e.g. informal norms, heroes and role models, rituals, stories and the specific language used to define important parts of the informal culture) and formal measures (such as a statement of the enterprise's core values, a compliance manual, a code of conduct or code of ethics, a mission statement and anonymous hotlines; see Belak Ja. et al., 2014; Murphy, 1995, 1998; Trevino et al., 1990, 1992, 1999, 2000; Laufer & Robertson, 1997).

At this point, it should be stressed that due to their different interests the company's stakeholders are considered constitutive elements of the business ethics and com-



pany's integrity at all levels. The examination of business ethics and the company's integrity exclusively at the mezzo level is therefore impossible since all three levels of business ethics and company integrity are tightly connected to each other and depend on each other. We therefore advocate the premise that only considering very narrow interpretations of the legal requirements cannot assure the company's ethical behavior or the building and sustaining of its integrity. For the purposes of integrity implementation, companies should overcome literal compliance with the law and, within a frame of their functioning, take into account purposes above the law (Di Lorenzo, 2007). Since the law is treated as a minimum ethical standard, it must not serve as the only basis for corporate ethics. The standardized and generalized behavioral requirements set by the law should therefore be supplemented by careful judgment and interpretation of the companies belonging to a certain industry.

At the micro level, the actions of an individual are observed and examined. The subject of research at this level is the functioning of an individual in his or her specific living environment and place of work and the circumstances that limit the individual's functioning in such a living environment (e.g. working conditions). The purpose is to describe what the individual's behavior ought to be in the case of an employer, manager or user. At this level, the possible behavior of an individual in particular conditions and circumstances is examined (e.g. the possible behavior of a co-worker who is concerned with the safety and quality of a certain product when superiors do not consider his or her arguments to be relevant). However, the core values and organizational culture can importantly influence an individual's behavior. In the company observed, the person responsible for complaints decided not to discuss the problem with the customer because the terms for the customer's claim had expired. The communication within the company on this particular matter was hidden to the researchers; therefore, we cannot argue that the decision was made solely by the responsible person or made under pressure from superiors (at the organization level).

At the mezzo level, the functioning of a company is examined and observed. A company consists of individuals who shape and form a certain entity or organization. However, such a company represents an economic unit; therefore, it should be considered an independent functioning subject. As such, it is responsible for its moral behavior and actions. It should also carry the burden as well as the consequences of its actions. In addition to being a legal entity, the company is also a moral entity; the company has moral responsibility for wrong actions. Therefore, in the case of unethical behavior, it should not only accept the legally assigned penalty, but also take other measures and responsibilities as well. The company examined in our research should (besides all legal requirements) be aware of ethical standards and consider the customer's expectations as well. The company should perform a careful audit of where and why the (ethical) conflict occurred. The responsible persons should be discovered and penalized. In relation to the customer, the company should take all responsibility for the actions of the responsible individuals and eliminate the occurred harm. Despite the fact that legally all terms for the customer's claim had expired, the company should replace the originally built (incorrect) materials with appropriate materials, those the customer ordered and paid for.

At the macro level, general economic conditions are shaped. At this level, questions regarding the best economic system for the functioning of different organizations such as companies, legal entities and consumer associations are established. In addition, this level considers questions such as the extent to which the market economy can satisfy ethical principles, what is the most righteous economic policy, how to set effective ecological and energy policies or how to set and implement a system of integrity in a certain economy. Our case study research shows that at the macro level the support for companies' integrity is insufficient. Therefore, it is necessary to develop and implement additional instruments for integrity implementation at the macro level, which will result in the companies' greater commitment to integrity. At this level of integrity, policy makers in Slovenia should consider the propositions of ISO 26000 as well as the OECD's (2009) guidelines to ensure an environment that fosters companies' ethics and integrity.

The observed company follows the regulations concerning the rights and obligations of customers (i.e. the customer) as well as the seller (i.e. Company X), which dictate that the window of time for possible customer complaints has passed; therefore, taking into account the legal frames of the customer's complaint, the company has no responsibility for the quality of the materials and/or services after the expiration of that time. In this case, we are taking into account the business ethics at the macro level where the legislation and legal questions are in focus. On the other hand, however, it is essential for the company's long-term existence and success to gain trust and develop integrity in the environment in which this company functions. Therefore, it should be in the company's interest to find out (even after the expiration of the guarantees) what in the company's relationship with the customer went wrong. Our case study research shows that the observed company refused even any dialogue concerning the described issues after the company realized that all legal notices had expired. After the dialog on the described issues and problems, the observed company should have carried out an internal audit, which would show that incorrect materials were used in the customer's house and consequently the customer's house is not of the quality that was guaranteed by the legally signed contracts and documents. This way, we conclude that even though the observed company may satisfy the macro level of business ethics, the company's behavior can be considered unethical taking into account the micro and mezzo level of business ethics. The observed company did not accept any responsibility for its actions that would foster clarification of the described issues. Rather, the observed company hid behind the legal frame of the business ethics approach to the customer rather than acting responsibly and credibly, in accordance with its integrity. Considering the above-stated elements, we can argue that the examined company would be more successful in implementing its credibility and integrity if it developed and implemented additional informal and formal measures for credibility and integrity.

### **3.4.3. Compliance of the Company's Behavior with the Law**

IN THE event of a construction defect, according to Slovenian law, the client has the right to take actions to enforce a guarantee. The actions to enforce a guarantee mainly refer to elimination of the defect. If the elimination of the defect incurs excessive costs, the

client may elect to request a reduction of the payment or a withdrawal from the contract. Furthermore, the actions to enforce a guarantee include the right of the client to compensation (a compensation claim) that may be exercised simultaneously with the actions to enforce a guarantee.

The action to enforce a guarantee regarding the general liability for defects is subject to a 2-year or, for a special type of liability for defects in the execution of the structure concerning its solidity, a 10-year time limit (Art. 634/2 and 662/1 of the OZ).

The client has the right to lodge a complaint with law enforcement authorities about the business fraud. If the time interval from the date of the commitment of the underlying criminal offence (i.e. business fraud) exceeds 10 years, criminal prosecution is no longer permitted due to the statute of limitations. The statute of limitations is 20 years for a qualified form (Art. 90/1 of the KZ-1).

In view of the provisions indicated above, in the present case, the client may no longer take actions to enforce a guarantee due to the expiry of the 2- and 10-year statutory time periods since the completion of the work, during which the contractor is liable for defects and the solidity of the structure.

Moreover, one may conclude that the criminal prosecution of business fraud is statute-barred. Criminal prosecution would still be possible if the damage caused to the client due to the contractor's failure to fulfil the obligation exceeded EUR 50,000.

The results of the legal analysis of the presented case study show that the client has exhausted all legal remedies to request the elimination of defects on the structure from the contractor, as the statutory deadlines for the enforcement have expired and the criminal prosecution due to business fraud is statute-barred. In other words, the company's behavior is in compliance with the law.

#### **3.4.4. Compliance of the Company's Behavior with Ethics**

HOWEVER, IF we take into account various models of integral management and governance (e.g. Sanktgallen's model of integral management, Hinterhuber's model of strategy management, Hunger and Wheelen's model of strategic management, the MER model of integral management and governance), we can state that the company would have to take actions which would lead to the clarification and rehabilitation of the occurred (ethical) conflict. We can therefore argue that to secure its long-term existence and success, a company must follow and obey ethical principles, not only legal principles.

We can state that the examined company has not acted ethically and that its integrity can be seriously endangered in the future. In facing the ethical dilemma, the examined company focused on the activities which would excuse it from taking responsibility for its own actions. Considering the macro level of business ethics as well as corporate integrity, it is true that the customer no longer has the right to use and practice any of the guarantees for the built materials. Also no institution (other than a court) at the macro level of corporate integrity existed where the customer could prove the ethical misconduct of the observed company.

## 4. Discussion

**T**HE CASE study research shows that corporate integrity is not an isolated phenomenon. The level of corporate integrity strongly depends on corporate governance and management. Thus, one can conclude that the concept of corporate integrity should be incorporated and implemented holistically within company management and governance process. Several models of governance and management have been established (e.g. Sanktgallen's model of integral management, Bleicher's model of integral management, the MER model of integral management) which emphasized the requisite holism of governance and management. For the discussion of the presented research findings, we refer to the MER model of integral management and governance (Belak Ja. et al., 2014). The MER model describes governance and management as having three dimensions: process, instrumental and institutional dimensions. Considering the process dimensions, the companies' integrity should be promoted and implemented (managed) at all management and governance hierarchical levels (political level, level of strategic management, and operational level) starting with owners and top management.

In this paper, we advocate the premise that the long-term existence and success of a company strongly depends on the company's credibility and integrity. Stemming from different models of management and governance, we argue that the company's owners and top management are the carriers of (and institutionally responsible for) a company's ethical and credible behavior and, consequently, the carriers of corporate integrity. A company's ethical behavior and integrity can be achieved only by "complete organizational conversion" (Thommen, 2003, p. 85), which has to take place at all levels of the company's management and governance processes (the political level, as well as the strategic and operational management levels). The idea of credibility and integrity should therefore be incorporated in a company's vision, mission and basic goals, strategy and finally the processes and structures needed for the realization of this idea of a credible company or a company with integrity. The strategic management process is where strategies are defined and the strategic allocation of resources is carried out to achieve the goal of making a company credible and achieving its integrity. The company's top management holds the main responsibility for these activities and they should result in a comprehensive ethics program indicating activities needed for the realization of a company's credibility and integrity vision, mission and strategies.

For the successful implementation of an ethics program to achieve the company's integrity, it is important that the program be internalized by all workers and groups and at all the company's management and governance levels. The integrity, credibility and ethical behavior of a company can be achieved only through holistic enterprise transformation and should be implemented from top to bottom, starting with the owners' values that influence the company's vision and policy (see also Thommen, 2003; Belak et al., 2014; Widana et al., 2015; Ferrel et al., 2011; Hassan et al., 2008) and ending with the fundamental (basic) realization process.

Considering the OECD (2008) guidelines, corporate integrity demands answers to “what,” “how,” “by whom” and “why” certain measures of corporate integrity should be implemented and assessed. This strongly supports the importance of management and governance basic functions (planning, organizing, directing and control/monitoring; Belak Ja. et al., 2014). The company’s integrity (implementation) should be well prepared and planned, organized, directed and controlled (monitored) at all management and governance levels. The theory and practice (as well as our research findings) show that at the declarative level many companies approach the problem of corporate integrity and/or business ethics. Furthermore, companies develop formal measures of corporate integrity implementation (e.g. codes, rules, guidance regarding integrity). However, they seem not to use them or to use them only when they find them suitable. If we take into account the levels of business ethics (and corporate integrity; Miller, 2007), we can say that these measures are mostly developed at the macro institutional level, but less so at the micro and mezzo levels. The implementation and management of corporate integrity should therefore consider not only the macro institutional level but also the micro individual and mezzo organizational level of corporate integrity as well. According to Maak’s “7Cs” of corporate integrity, such contradictions arise particularly because sufficient “consistency” in the process of corporate integrity implementation is missing. Our case study research shows that the possibility of implementing sanctions and benefits for participating stakeholders at all levels of corporate integrity should also be considered. Miller (2007) pointed out that integrity systems should have sanctions for those who do not comply with legal rules and ethical standards and also benefits for those who act in compliance. Today, this stick-and-carrot approach is popular, but both of these “self-interest” reasons for compliance must be connected with a moral sense to do what is right (Miller, 2007, p. 359).

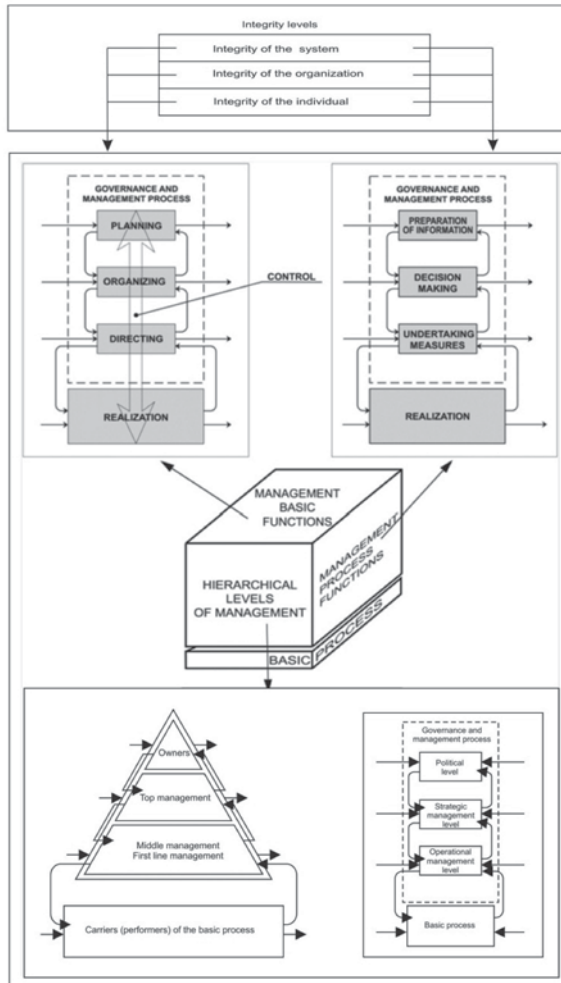
This way, the management and governance of corporate integrity considers also the individual’s moral judgments in facing ethical dilemmas at the mezzo organizational level of corporate integrity and overcomes the minimum ethical standards as set and defined at the macro institutional level of corporate integrity.

We therefore argue that it is not sufficient to plan, organize and direct the company’s integrity. Considering the MER model of integral management and governance, the control of activities and achievements should be carried out constantly as one of the basic functions of the management and governance process (Belak Ja. et al., 2014). To successfully carry out the controlling (monitoring) process at all hierarchical levels, adequate controlling instruments (measures) should be developed (compare with Belak et al., 2010). In a context of companies’ integrity monitoring, the OECD (2008) refers to passive monitoring, with the setting up of reporting channels, and active monitoring, with various measures such as whistleblowing (compliance officers, internal auditors), survey measurement of integrity violations and integrity dilemmas and informal probing for ethical dilemmas and issues among staff. The OECD has also proposed measures on the macro level of corporate integrity, like citizen complaint systems such as ombudsmen, where citizens can complain about wrongdoing by companies or individual company employees.

The main goal of an integrity system and its basic elements (ethics, codes of conduct, education programs) is not to dissuade the minority of wrongdoers from doing bad but to convince the majority to be sensitive to wrongdoing. In this context, it is worth pointing out that most fraudsters are detected and convicted as a consequence of disclosures from their colleagues (Miller, 2007, p. 369).

We therefore argue that all basic functions (planning, organizing, directing and controlling) and dimensions (process, organizational and institutional) of management and governance of companies' integrity should be carried out at all three levels of corporate integrity (micro, mezzo and macro), as shown in Figure 1.

Figure 1. Integrity levels in relation to the governance and management process.



In this discussion, we argue the importance and (especially) the lack of a controlling and monitoring function in the corporate integrity management and governance process. As conceptualized within the MER model, each function has its institutional and instrumental dimension. It is therefore of crucial importance to guarantee the successful implementation of corporate integrity by its institutionalization as well as instrumentalization. Both must be controlled and monitored (especially) at the macro (institutional, system) and mezzo (organizational) levels of corporate integrity. At the macro level, institutions or bodies should be established and implemented (by the state authority). Their basic function should be to control and monitor the compliance of companies' behavior with the adopted ethical standards at the level of the economic, social and political system. At the mezzo level, the companies themselves should develop and implement institutional measures to foster and control (monitor) the integrity of their (as well as individuals' and company stakeholders') behavior. In this case, the control and monitoring at the macro level of corporate integrity would use an external audit of corporate integrity, where control and monitoring at the mezzo level of corporate integrity would use an internal audit of corporate integrity. In our opinion, such a holistic approach in accordance with the dimensions and basic management and governance functions would result in a successful corporate integrity implementation.

However, our case study research clearly shows that prescribed monitoring and existing audit mechanisms cannot prevent all possible risks to the holism of corporate integrity, particularly at the micro and mezzo levels. Besides strengthening the external and internal measures of monitoring and auditing the system of corporate integrity, steps for evaluating the behavior (i.e. stick-and-carrot approach) of each participating individual should also be incorporated as an integral part of the corporate integrity system (at the mezzo and macro levels of corporate integrity). In this way, the individuals, stakeholders and companies would behave more ethically. In our opinion, such a holistic approach to corporate integrity would lead to more efficient and effective systems of corporate integrity and result in higher levels of corporate integrity.

## 5. Conclusions

**I**N THE long run, top-performing companies will be those ensuring not only their regulatory compliance but also their compliance with ethical standards. As we have seen from our case study, the conduct of a company, even though it is in compliance with laws, rules and regulations, does not necessarily ensure the satisfaction of other stakeholders if it fails to comply with ethical standards. The law is a relatively rigid system of rules that roughly regulates the most important relationships in a society and protects its most important values. This is why it is created prudently, in an organized manner, although it cannot regulate in detail all forms of social life. Therefore, it is important for legal rules to complement ethical standards, being more or less constant and close to people in terms of their content, thus making them easier to accept and respect. A symbiosis of legal and ethical rules is crucial for all forms and at all levels of organized association of individuals, including corporations and companies. Therefore, corporate

integrity, in our view, is crucial to ensuring such symbiosis or “wholeness” of a company. The concept of corporate integrity is correctly defined, although in practice its major drawback is the absence of supervision and control over the implementation (provision) of corporate integrity in a company.

To address this weakness, actions are required at the macro level, with the state playing a major role to set up supervision and control mechanisms through its own means. It is too soon to say whether the state will use its legislative power or opt for softer forms of control mechanisms. Nevertheless, the state instrumental and institutional framework is essential for efficient corporate integrity in companies. Our case study research shows that if institutional measures of internal and external audit of corporate integrity existed, the presented ethical dilemma would be handled in a different and more effective way.

On a mezzo level, it would be necessary to raise awareness of the significance of corporate integrity among individuals and stimulate them to help provide corporate integrity in their company. In this context, it would be necessary to explore whether a carrot-and-stick method would be suitable for it or any other type of stimulation.

In our opinion, the implementation of corporate integrity requires a multifaceted approach to accommodate different cultural and economic characteristics that vary from country to country, from continent to continent. This needs to be taken into account in any further exploration at all levels of ethical relationships. In other words, when building a corporate integrity system, both legal and ethical issues must be addressed. □

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## Abstract

### Corporate Integrity: Just a Concept or Real Behavior/Practice

Numerous scandals in many companies resulting from the unethical behavior of key stakeholders have brought to the fore the importance of the concept of corporate integrity and its application in governance and management processes. Different guidelines and recommendations have been established, whose main purpose is to help companies achieve and sustain credibility and integrity. The case study research methodology was applied to explore the concept of corporate integrity in practice. We used an extreme case to show that, on the one hand, corporate integrity is a relevant phenomenon but, on the other, it needs changes in order to improve companies' practices. Several proposals are presented in the paper based on the legal and ethical analysis of the case.

## Keywords

corporate governance, corporate integrity, business ethics, case study