THE UNIVERSITY OF
SYDNEY

The Business & Professional Ethics Group in conjunction with the Natoli Ethics Fund

Student Ethics Essay Prize 2017
(undergraduate)

This certificate is awarded to

Hasan Mohammad

in recognition of the best essay submitted by an undergraduate student.

10 November 2017

Category 1: Undergraduate students
The category 1 essay contest is open to any student currently studying a business degree or unit at undergraduate level within the University of Sydney Business School. The best essay will be chosen for a $1,000 cash prize.

The Case for Naked Business:
Reflections on Transparency and the Wells Fargo Scandal

Hasan Mohammad

The Panopticon was the perfect prison. Originally conceived of by the father of utilitarianism, Jeremy Bentham, it represents a deep-seated truth about human nature: our propensity to modify our behaviour while we are being watched. The imagery of Bentham's architectural idea is striking; he envisaged a warden in a central tower surrounded by cells. The tower shines bright light so that the warden can see the inmates inside the cells. Because the inmates, however, are not able to see the warden, they must assume that they are always under observation, creating a "sentiment of an invisible omniscience" (Bentham, 1843).

Internalising within employees the presence of an "all-seeing eye" seems like the goal of most modern workplaces. In an attempt to reconstruct something like Bentham's Panopticon, major corporations invest billions annually (Gartner, 2015) in surveillance technology, internal control procedures, IT measures and security departments to achieve something of a self-disciplining ideal in the workplace. The hypothesis is simple: we behave more ethically when we think we are being watched. But to what extent does this premise represent reality? In principle, should transparency increase ethical behaviour? And does it achieve that goal?

While there is no universal definition of transparency in the business setting, most accounts essentially boil down to the notion of information visibility. Turilli and Floridi (2009) define transparency in terms of "the possibility of accessing information, intentions or behaviours that have been intentionally revealed through a process of disclosure". This definition is manifestly neutral in its ethical content but serves as a precondition for ethical behaviour, when the disclosed information has an impact on ethical principles, such as honesty, integrity and accountability.

The recent Wells Fargo account fraud scandal provides a springboard for an updated view of the status of transparency in the 21st century workplace. After positioning itself among the largest and most respected American banks in a post-GFC era, Wells Fargo subsequently fell from grace when it was implicated in fraud. 113 pages of analysis revealed how between 2011-2015, Wells Fargo employees created 2 million deposit accounts and issued over 550,000 credit cards on behalf of clients without their consent (Board of Wells Fargo & Company, 2017). Many clients were then charged fees on such accounts, which were then followed up by official debt collection agencies. Many accounts were subsequently subjected to "pinning", a process in which personal-identification numbers (PINs) were assigned to them to impersonate clients, enrolling them in further services without their knowledge. Following extensive investigations, in September 8, 2016, Wells Fargo agreed to pay a $185 million fine to various regulatory bodies and 5,300 staff have since been fired over their role in the scandal (Tayan, 2016).

One cannot help but be enthralled by the sheer scale and magnitude of such a fraud. Does it challenge or confirm conventional wisdom on the need for transparency?

The scientific literature is rife with examples of how even the illusion of being watched can shape ethical decision making. Bateson and Nettle (2011) performed an experiment demonstrating that hanging posters of staring eyes is conducive to the promotion of cooperative and ethical behaviour. In their test, they examined the incidence of littering in a cafeteria, counting the number of people that cleaned up following their meals. The location of the poster was altered each day and the researchers discovered that during periods when the posters of eyes, instead of a control like flowers, overlooked the cafeteria patrons, twice as many people cleaned up after themselves.

This effect has been attributed to the phenomenon of "gaze detection" (Haxby et. al., 2000) which played a role an evolutionary role in predator detection and processing of information provided by facial expressions. In a similar experiment (Bateson, Nettle, & Roberts, 2006), they hanged posters of eyes and of flowers near a box in which people deposited contributions to a coffee fund. The eye images had a significant effect, with average contributions increasing threefold in weeks when eyes were shown compared to when flowers were shown.

So how was it so easy for so many Wells Fargo employees to break the rules? Transparency ultimately depends on an ethical business culture and a feasible system of checks and balances (Zhu, 2004). By perpetuating a culture of "cross-selling"; in which the bank placed pressure on employees to sell multiple financial products at a time, Wells Fargo inadvertently incentivised fraud. Ambitious sales targets were reinforced by any daily shortfalls being added to the following day's targets and bankers received bonuses of up to 20% of their salaries when such quotas were achieved (Tayan, 2016).

A study by Brunner and Ostermaier (2017) bears many parallels to the Wells Fargo scandal. They examined the practice of "slack creation", which is a form of deceptive reporting whereby managers overstate the actual cost of a budget, often well over the minimum needed for a task, to create excess resources for their own benefit. Their results revealed an asymmetric correlation between the degree of deceptive reporting and the degree of transparency. The effects of dishonesty were found to exceed that of honesty as managers exploited peer dishonesty to justify their own. Managers' slack thus increased when peers' reports are higher than expected but decreased little when they were not. Partial transparency compared to under full transparency produced a larger asymmetry, as partial transparency allows managers to complement missing information with self-serving assumptions: when they lacked knowledge of their peers' costs, they simply attributed higher valued reporting to dishonesty instead of high costs. Hence, managers increase their slack under partial transparency more readily than under full transparency in the case where peers' reports exceed expectations. Consequently, in an environment like Wells Fargo, a "slacking culture" thrives and perpetuates a cycle of wilful deception.

All in all, corporations must strive to incentivise naked business i.e. business that is open and fosters a culture of accountability to complement standard internal control procedures. Wells Fargo is one of countless examples of what happens when this process is compromised.

References

Bentham, J. (1996). *The collected works of Jeremy Bentham: An introduction to the principles of morals and legislation*. Clarendon Press.

Turilli, M., & Floridi, L. (2009). The ethics of information transparency. *Ethics and Information Technology*, *11*(2), 105-112.

Tayan, B. (2016). The Wells Fargo Cross-Selling Scandal.

Ernest-Jones, M., Nettle, D., & Bateson, M. (2011). Effects of eye images on everyday cooperative behavior: a field experiment. *Evolution and Human Behavior*, *32*(3), 172-178.

Haxby, J. V., Hoffman, E. A., & Gobbini, M. I. (2000). The distributed human neural system for face perception. *Trends in cognitive sciences*, *4*(6), 223-233.

Bateson, M., Nettle, D., & Roberts, G. (2006). Cues of being watched enhance cooperation in a real-world setting. *Biology letters*, *2*(3), 412-414.

Zhu, K. (2004). Information transparency of business-to-business electronic markets: A game-theoretic analysis. *Management Science*, *50*(5), 670-685.

Brunner, M., & Ostermaier, A. (2017). Peer influence on managerial honesty: the role of transparency and expectations. *Journal of Business Ethics*, 1-19.

Gartner Inc. Forecast Analysis: Information Security, Worldwide, 2Q15 Update (2015)

Independent Directors of the Board of Wells Fargo & Company Sales Practices Investigation Report (April 10, 2017)