



## Acknowledgement

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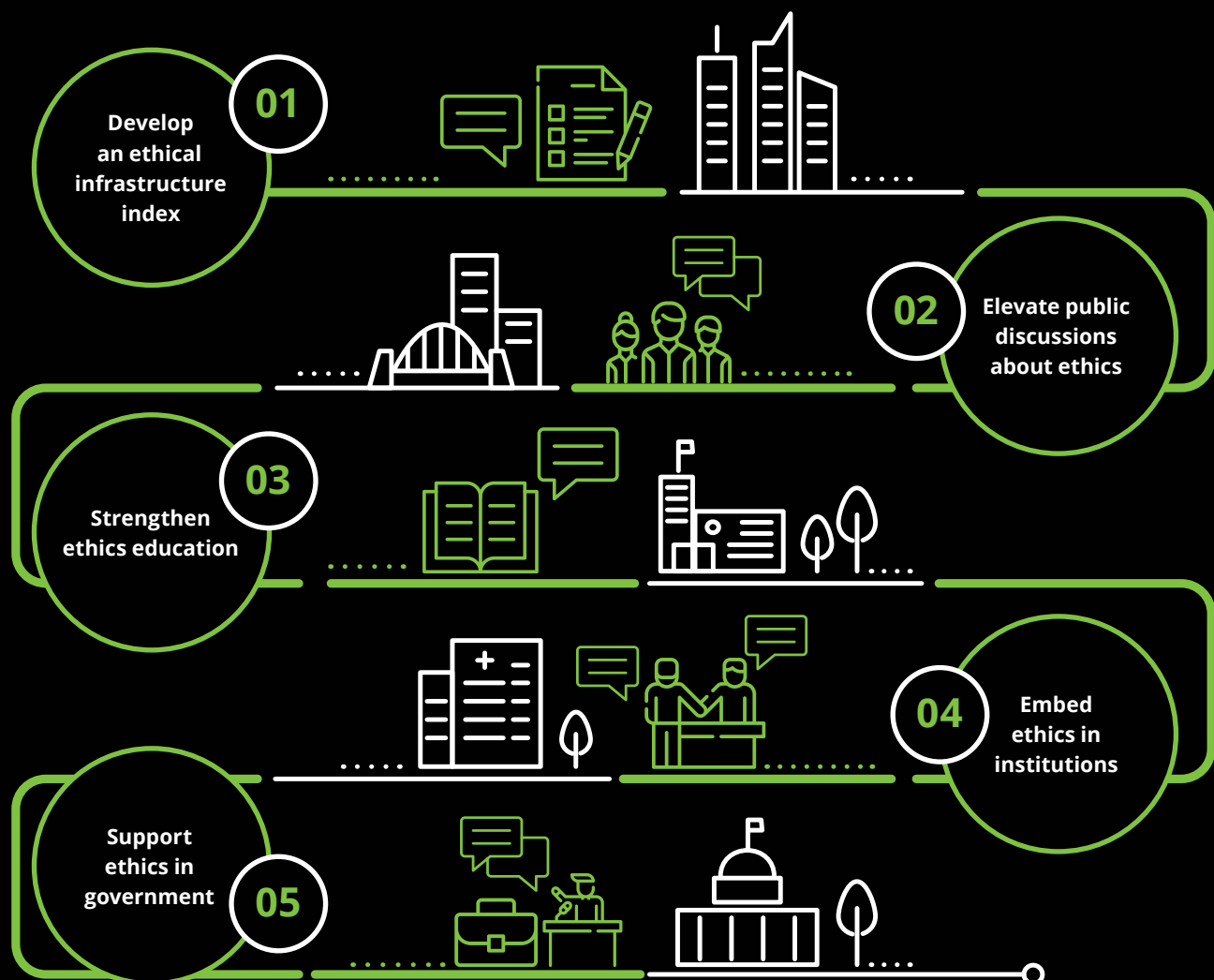
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# The ethical advantage: the economic and social benefits of ethics to Australia

Ethics is a way of structuring human reasoning to help choose what is right or best

How do we build a more ethical Australia?





## Just how ethical is Australia?



Proportion of Australians who think most people can be trusted



Average assessment of the degree to which others make agreements honestly, keep their word or succeed by not stepping on other people



The Governance Institute rates Australia +37 on a scale of -100 to 100. The health care sector is seen as the most ethical.

## Ethical infrastructure can be built at the society or organisational level, in both formal and informal ways...if we could it would help



### Individuals

By improving their mental health and wages.

A **10%** improvements in ethical behaviour is associated with a **1%** improvement in mental health and a **2.7%** increase in wages.



### Businesses

Improving a business' ethical reputation can improve its relationships with customers and suppliers and can lead to a 7% increase in return on assets.



### The economy

Improving trust and social capital allows for the smoother functioning of markets and reduces the cost of regulation and compliance.



### The bottom line

Lifting Australia's trust levels to that of the global leaders would increase GDP by:

# \$ 45 billion



# Executive summary

At the dawn of the third decade of this century, Australia faces significant challenges – navigating the health and economic impacts of the COVID-19 pandemic, responding to emerging issues around the future of work and introduction of new technologies, preparing for an increasingly risky geo-political environment and addressing long-standing social and environmental challenges including climate change, and reconciliation with Indigenous Australians.

Addressing these issues will require effort from many organisations, businesses, community groups and government bodies, and will draw on a range of competencies and technical skills. Inevitably, we will need to make some ‘big decisions’ – and this will require leadership of a quality that enables society to cohere in the face of external and internal pressures that would otherwise cause divisions. In these circumstances, trust will be at a premium – especially for key institutions. In turn, this will depend on the quality of ethical decision making by individuals, groups and organisations.

There remains significant scope for Australia to lift our levels of ethical behaviour and trust. In 2019, Australia was rated as being only ‘somewhat ethical’, achieving an index score of 37 on the Governance Institute of Australia’s -100 to 100 scale, four points down on the result two years earlier. The banking sector, which all Australians rely on, was considered the most unethical industry.

When asked whether people keep their word or make agreements honestly, everyday Australians say ‘yes’ ... but do not hold this view with great confidence – with an agreement score of around 12 out of 18 on the Household, Income and Labour Dynamics (HILDA) survey. According to the World Values Survey, just 54% of Australians state that they generally trust other people they interact with. While this might be a higher score than achieved by many countries, including the USA and UK, the Australian score is 10 percentage points behind the world leader.

In some respects, Australia’s relative ethical performance is no surprise. A steady stream of state and federal political scandals has eroded trust. Royal Commissions have uncovered: unconscionable behaviour in religious and other institutions, widespread misconduct in the banking, superannuation and financial services industry, and most recently, alarming activities relating to aged care quality and safety.

Australia’s uneven ethical performance is also evident in corporate culture. A 2018 review found that while almost all ASX200 companies disclosed a code of practice, only six per cent had leading practice. The rest were either infrequently updated or had little CEO buy-in; two-thirds did not contain even five of 13 recommended topics.

While few would argue a higher level of ethics in individuals or institutions is a bad thing, articulating the benefits of stronger ethics is more challenging. For this reason, The Ethics Centre commissioned Deloitte Access Economics to develop a framework to quantify the benefits of a more ethical Australia: how, and by how much, would individuals, businesses and the economy be better off were Australia to have, say, the best ethical performance in the world? This project is not intended to reduce ethics – the very question of what is right and wrong for us as humans – to a mere dollars-and-cents business case, but rather to put a financial analysis alongside the moral case for change, in order to strengthen it.

Reviewing many data sets, research sources and performing three new types of economic modelling, the results are in:

- Individuals would benefit from improved mental and physical health, avoiding the costs associated with the 'moral injury' caused by unethical decisions. Consistent with this, the impacts are larger for mental than physical health with a 10% improvement in individual perceptions of others' ethical behaviour associated with a 1% improvement in perceptions of their own mental health. The Productivity Commission estimates a \$130 billion cost associated with diminished health and reduced life expectancy for those living with mental ill-health. Even a 1% improvement in mental health outcomes could have significant implications for the economy and individual well-being.
- There is also a business case for being ethical. While there are a range of moral reasons for a business being ethical, there is also evidence that unethical behaviour leads to poorer financial outcomes for business. This study supplements the literature in this area by drawing on data from the RepTrak Governance Index (a measure of ethical perceptions), which shows a positive association between return on assets and performance on the Governance Index. Increasing a firm's performance on the Governance Index by one standard deviation raises return on assets by approximately 7 per cent or around 50% for those firms in the sample.
- There is also evidence that individuals would enjoy higher wages consistent with an improvement in labour and business productivity. Specifically, a 10% increase in regional measures of ethical behaviour was associated with an increase of 2.7% to 6.6% in individual wages. A 2.7% increase in wages would amount to approximately a \$23 billion increase in aggregate wages across the economy.
- The economy can benefit from smoother functioning of markets and lower costs of regulation and compliance. If Australia was to improve ethical behaviour, which in turn led to an increase in trust, in line with the world's leading countries, average annual incomes would increase by approximately \$1,800. This equates to a net increase in total incomes across Australia of approximately \$45 billion. These annual benefits would grow towards these levels as the country moved towards higher levels of trust.

These estimates capture the potential economic gain from improving ethical behaviour and do not explicitly account for any costs associated with programs or initiatives to improve ethics in Australia. There are also overlaps between many of these outcomes such that they are not additive. For example, improvements in business return on assets or productivity and employee wages are captured in GDP.

Nonetheless the results indicate that there are likely to be large economic dividends from improving ethical outcomes. To put it in perspective, a more ethical Australia would achieve an economic improvement about half as big as the nation's economic reform priority list outlined by the Productivity Commission in 2017, where 28 reforms would lift the economy by some \$80 billion over time.

Ultimately, improving ethics requires a multifaceted and coordinated approach. The complexity of ethical decision making, and the infrastructure needed to support it, means improving ethics cannot be achieved with a single initiative. Recognising these inherent challenges, there are a number of potential initiatives which can help improve ethics in Australia. This report identifies five areas for improvement, supported by 30 individual initiatives.

1. Developing an Ethical Infrastructure Index
2. Elevating public discussions about ethics
3. Strengthening ethics education
4. Embedding ethics within institutions
5. Supporting ethics in government and the regulatory framework

The report concludes with a discussion of how a stronger ethical framework based on these development areas could inform a response to three key challenges in Australia – reconciliation with Australia's First Nations people, climate change and the environment, and technology and artificial intelligence.

Overall, with the individual, business and economic benefits on offer from a more ethical Australia, the business case for change is a sound one. With the challenges facing the country, strengthening ethics is simply a must.

# 1. Introduction

At the dawn of the third decade of this century, Australia faces a number of significant economic and social challenges. On the immediate horizon, the country must navigate its way through the COVID-19 pandemic and the aftermath of recent bushfires to minimise both the health and economic impacts. While dealing with this unprecedented situation, the country must also prepare for other changes, including how work and workplaces are changing, and how best to manage the introduction of new, useful (but radically transformative) technologies.

Beyond this horizon there lie a number of broader social and environmental challenges. Climate change is Australia's most significant challenge to the natural environment, but there are others relating to: resource use, water supply and protection of biodiversity. The social environment is equally demanding. Australia's ageing population is putting increased pressure on social security, health and aged care sectors. Inequity is a huge problem in Australia, especially for Indigenous Australians that, on average, face circumstances vastly different from non-Indigenous Australians.

There are no simple solutions to any of these challenges. Each will demand 'big decisions' to be made; supported by sound leadership and wider community participation. Some issues will require national coordination. Others will best be resolved at a regional or local level. While governments will have a role to play, their efforts will need to be complemented by those of businesses, not-for-profit and civil society institutions. Invariably, there will be important ethical issues that will have to be addressed in a manner that inspires community trust and confidence. In the absence of trust and confidence, any resolution of the looming issues, before us, will be sub-optimal.

This report examines the case for improving ethics as a way of addressing these broader economic and social challenges – and the nature and extent of the benefits that would accrue to the nation from doing so.

Across a number of indicators it is clear that there is scope for improving ethics and consequently trust in Australian society. According to the 2020 Edelman Trust Barometer, Australia's institutions are currently falling short in building trust among Australians. Just 47% of Australians trust business, government, media and our NGOs to do the right thing. Worse still, none were seen as strongly competent or ethical – with government being seen as the least competent and ethical out of all our institutions.

Other measures of ethical behaviour, such as those compiled by the Governance Institute and the Household, Income and Labour Dynamics in Australia (HILDA) survey, indicate that there remains significant scope to improve ethical behaviour in Australia, as highlighted in the next page.

# How ethical is Australia?

The Governance Institute of Australia's Ethics Index is an annual national survey, measuring Australians' perceptions of the level of ethical behaviour in society.

- In 2019, Australia achieved an overall index score of +37 ("somewhat ethical") on a scale between -100 and +100. This was an improvement on the score of +35 in 2018, but represented an overall decrease compared to the all-time high score of +41 achieved in 2017.
- Across different industries, Health was seen to be most ethical industry with an index score of +67. This was followed by education, charities and not-for-profit organisations, then agriculture. Banking, finance and insurance was seen to be the least ethical industry with an index score of -18.

The Household, Income and Labour Dynamics (HILDA) survey is another annual, nationally-representative survey, which is funded by the Australian Government through the Department of Social Services. Since 2001, it has collected data on perceptions of ethical behaviour by asking respondents whether they agree with the statements that: "Most people keep their word", "Most people make agreements honestly" and "Most people you meet succeed by stepping on other people".

- Most Australians have tended to weakly agree with the three statements, with a total mean score of 11.7 out of 18.
- On average, older Australians (aged 60+) have tended to perceive higher levels of ethical behaviour around them, relative to younger age groups. Those aged between 20 to 29, for example, registered the lowest average total score out of all age groups at 10.9, while those aged between 80 and 89 had the highest average total score of 13.3.
- Women consistently believe there to be higher levels of ethical behaviour in Australia, with an average total score of 11.9, compared to men with a score of 11.5.
- Perceptions of ethical behaviour appear to be strongest in Greater Western Australia with an average total score of 12.1.

Internationally, more reliable statistics are available for measuring trust (which is different to, but is strongly affected by, levels of ethics). According to the World Values Survey, 54% of Australians stated that they generally trust other people that they interact with. This was a considerably higher percentage than the USA, the UK and most Western European nations but some way behind the Scandinavian countries of Sweden, Norway and Finland. In particular, we were approximately 10 percentage points behind Sweden – a country with consistently one of the highest levels of trust.

Australia's uneven ethical performance is also evident in corporate culture. A 2018 review found that while almost all ASX200 companies disclosed a code of practice, only six per cent had leading practice. The rest were either infrequently updated or had little CEO buy-in; two-thirds did not contain even five of 13 recommended topics. Whistleblower policies, critical to ethical performance, were patchy too, with many ASX200 businesses not having the key features of anonymity, 24/7 access, supplier/contractor access and anti-retaliation measures.<sup>1</sup>



Findings that ethics and trust have weakened in Australia are perhaps not surprising. The last few years have seen the emergence of evidence of serious ethical failures in Australia, the most-high profile of which have resulted in Royal Commissions, including:

- *The Royal Commission into Institutional Responses to Child Sex Abuse*
- *The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry*
- *The Royal Commission into Aged Care Quality and Safety.*

Adding to these issues have been an ongoing series of scandals in Federal and State politics. These issues highlight the ethical challenges Australia is facing now. Improving ethical behaviour not only holds the promise of helping minimise future ethical failure but will underpin (and hopefully rebuild) trust levels that will be necessary to address future challenges.

It is against this background that The Ethics Centre engaged Deloitte Access Economics to examine the economic case for improving ethics in Australia and inter alia to examine the degree to which improving ethics may help address Australia's longer term economic and social challenges.

The report builds on the many previous research efforts on ethics and economic performance, drawing insights from over 50 reports. The economic modelling uses data from many public and private sources including: the ABS, World Bank, World Values Survey, RepTrak, IBISWorld, and HILDA. The authors of the report also gained insights from interviews with a range of public and private sector leaders familiar with ethics and economic performance, including:

- **Grant Hehir**, Auditor General of Australia
- **Maria Milosavljevic**, Chief Data Officer at Services Australia
- **Ian Harper**, Dean of Melbourne University Business School
- **Glenn Stevens**, Former Head of the Reserve Bank of Australia
- **Kate McClymont**, Investigative Journalist
- **Mara Bun**, President of the Australian Conservation Foundation
- **Michael Barnes**, New South Wales Ombudsman
- **Andrew Scipione**, Former Commissioner of the New South Wales Police Force
- **Hugh Breakey**, President of the Australian Association for Professional and Applied Ethics
- **Nev Power**, Head of the COVID19 Coordination Commission
- **Megan Motto**, CEO of the Governance Institute of Australia
- **Dr John A. Rees**, Professor of Politics & International Relations at the University of Notre Dame Australia

Chapter 2 discusses the key concepts of ethics and ethical infrastructure. Chapter 3 outlines an economic framework for analysing the benefits of ethics and presents the results of new modelling undertaken for this project. Chapter 4 outlines ways in which Australia can strengthen its ethical infrastructure over time.

## 2. Ethics and ethical infrastructure

### 2.1 What is ethics?

The field of ethics seeks to understand and inform the underlying structure of human choice. As such, it deals with one of the most potent forces on the planet. Ethical reasoning helps people navigate complexity and to choose a path that is right or best, given the alternatives. It helps answer the question, ‘what am I to do?’ by reflecting on things like our values (what is good), principles (what is right) and purpose (why we exist).<sup>2</sup>

Ethical decision making is a process that improves decisions.<sup>3</sup> It liberates people from the confines of unthinking custom and practice by enabling the conscious application of core values and principles. Ethical decision making ranges from the deployment of whole systems of thinking to the use of convenient ‘ready reckoners’ in the form of questions like: ‘would I be happy for this decision to be headlining tomorrow’s news?’ or ‘what would happen if everyone did this?’<sup>4</sup> Religions also seek to guide thinking about how to act in different situations by declaring what is right, wrong, good and bad.<sup>5</sup> To that extent, religions and ethics overlap – with the former covering additional ground dealing purely with theological questions. Although there is a measure of overlap, ethics and religion can operate independently. It is not necessary to hold religious beliefs in order to live an ethical life.

Ethical decision making is particularly helpful when trying to resolve apparent ethical dilemmas – when equally valid values or principles compete. Consider the example of border protection policy, where mandatory offshore detention has a deterrent effect on potential asylum seekers who would otherwise risk their lives on the high seas but also has significant negative impacts on those held offshore.

However, ethical issues easily shift from the ‘macro’ to the ‘micro’ in ways that affect daily life. In some countries, medical staff have been required to ration access to ventilators in circumstances where patient demand has exceeded available supply. Deciding who lives and dies not only risks causing ‘moral fatigue’. It can also lead to ‘moral injury’ – especially when there is insufficient time (or experience) to apply sound ethical decision making practices. In turn, the fatigue and injury can further reduce the supply of health-care workers – further exacerbating the underlying problem in a vicious spiral. While solutions to these challenges are not straight forward they inevitably involve ethical decision making and an increase in ethical decision making capacity can help reduce moral injury.

Individuals in Australia have been offered a choice about whether to download the COVID-safe app or not, weighing up issues about community responsibility against privacy concerns amongst some. As is so often the case, competing values can leave people ‘stuck’ – when a more productive outcome could have been achieved if only there was a more general capacity to reason about the ‘everyday’ ethics of life.

The need to address ethical tensions will not end when COVID-19 is brought under control. They will extend into the recovery phase. As the Head of the COVID19 Coordination Commission, Nev Power, notes:



“There is an ethical tension between promoting the welfare of people today by creating employment in sectors like natural resources, and thinking about people of the future and the protection of our environment more generally. These considerations must be balanced, and there is often a middle way that can be found between competing interests.”

As noted above, ‘being ethical’ does not require a complex understanding of philosophy.<sup>6</sup> What is more important is the process of reflection and thinking, and being sensitive to the ways in which a person’s context structures choice. In the absence of conscious deliberation, the decisions people make are more often shaped, uncritically, by their environment or based on emotional, gut responses, rather than objective, rational analysis.<sup>7</sup>

However, what if we could shape the environment so that it encouraged and supported better decision making? While there are common underlying ethical sensibilities that cross cultural and temporal barriers – such as a positive regard for being honest, respectful and fair – ethics can and do vary according to context. For example, the same value or principle can be expressed in different forms of behaviour, or values and principles can vary in relative priority. As an example of the former case, consider the value of ‘friendship’ that in some contexts is expressed through informal means – such as spending time together. In other contexts, the same value of friendship can be expressed by formal means – such as the giving of gifts or other ritual tokens of esteem.

What is true for major cultures also applies in the workplace – where particular contexts can be linked to distinctive frameworks of ethics. For example, some occupations have their own codes of ethics which, amongst other things, confer specific duties and obligations on their members, often monitored by a governing body. These codes come under the umbrella term of ‘professional ethics’, and while there is not a strict definition classifying some occupations as ‘professions’ and some not, it is generally understood that to be professional is to be more than an expert skilled in the provision of vital services. Rather, the hallmark of a profession is that it requires its members to subordinate self-interest and instead to act in the best interests of others (e.g. clients).<sup>8</sup> Professionals often operate in a regulatory environment where ethical commitments are reinforced by formal, legal obligations. Where professions differ from each other is in terms of the ‘defining goods’ they are meant to serve. For example, lawyers are supposed to have a particular care for the administration of justice. Journalists should be especially concerned about truth. Doctors and other health care professionals should work to promote human health and well-being.



# Perspectives on ethics

“Ethical decision making in the public service means being rigorous and transparent in one’s decision making, and understanding the responsibility government has to the public it serves.”

**Grant Hehir, Auditor-General**

“Ethical decision making as a journalist requires thinking about the consequences of the person you are writing about and putting information into proper context. Every story has ethical dilemmas, and requires thinking about have I been fair, spoken to enough people, have I omitted any crucial facts etc.”

**Kate McClymont, Investigative journalist**

“Ethical decision making for police officers means understanding their role as community stewards, and acting within and for the community at all times.”

**Andrew Scipione, Former commissioner of NSW Police Force**

“We all have values and moral convictions – ethics is about having the courage to apply these in the real world.”

**Professor Ian Harper**









## 2.2 Ethics, law and trust

Ethics is not just about individual decision making but is an important foundation for many of our social institutions, including markets and law. Ethics is critical to underpinning transactions in the economy – particularly where product quality (or in the case of services, effort) is not perfectly observable to those transacting. In this respect, ethics can help overcome issues of imperfect information, which can undermine the benefits of competitive markets. As noted below, Adam Smith, understood that markets can only be considered ‘free’ if they are built on an ethical foundation.

Important social values like trust, respect, transparency and fair competition are unimaginable without strong ethical relations between people in society.

Ethics also underpins an individual's willingness to adhere to the rule of law. In the absence of ethical behaviour, governments would need to invest considerably more in monitoring enforcement of the law and equally monitoring those who monitor enforcement of the law.

One of the most important outcomes of high ethical standards in society is high levels of trust. Here, we define trust as a belief in the reliability or truth of someone or something. This can encompass interpersonal trust, institutional trust, trust in government or trust in technology.<sup>9</sup>

High levels of trust simplify daily life – trusted institutions are the “grease in the social machine” as Tarun Khanna argues.<sup>10</sup> In contrast, low trust in institutions carries costs, including that of individuals being less likely to comply with laws and regulations, pay taxes, tolerate different viewpoints or support their neighbours.<sup>11</sup> Additionally, a lack of trust can make people wary of embracing change – even if the change might benefit them – for fear of being overlooked and disadvantaged. Trust inspires collaboration, creativity and innovation, contributing to economic vitality; a lack of trust leaves societies fragmented and more susceptible to chaos and conflict.<sup>12</sup> In *The Wealth of Nations*, Adam Smith outlines how in an ideal market situation, two people can trade and become better off despite neither person being motivated by benevolence. The ‘invisible hand’ operates so that the self-interest of each is converted into the good of the other. And to do this effectively, markets require an ethical foundation which produces trust.

Social cohesion and the effective functioning of our democracy depends on ethical values like trust and respect between people. Enforcement mechanisms, like the legal system, encourage and shape behaviour. However necessary they might be, they are not sufficient. In reality, laws mostly tell us only what not to do, not how to act. Ethics – governing the way people treat each other – provides the ‘social lubricant’ for laws to work effectively and for markets to function.

In the international arena, ethics and trust can play an important role in strengthening trading and diplomatic relationships between countries. As a successful trading nation, Australia has a strong interest in building trust among its trading partners and the preservation of a stable, rules-based international order. While ethical behaviour can potentially reduce the need for extensive rules and regulations, in the international arena a rule based international order serves to constrain unethical behaviour by reducing the temptation for unilateral action that is in a state's interest but imposes costs on other states or reduces trust in international relations. That order is currently under threat – in part due to the changing domestic priorities within countries and in part due to rising tensions associated with major power rivalry – especially within Australia's immediate region. These tensions are testing the resilience of alliances and are exacerbated by the effects of cyber threats. Developing national resilience and strong internal ties, based on shared ethical values and principles, can potentially assist Australia to project ‘soft power’ into our region.

## 2.3 Ethical infrastructure

What if we could **shape our systems and environment to encourage ethical behaviour and inhibit unethical behaviour**, including by making environments that are more conducive to ethical reflection? Those systems and the associated environment are captured in the concept of ‘ethical infrastructure’. Ethical Infrastructure encompasses the structures and institutions that help foster ethical decision making, in governments, businesses, other organisations and within broader society.

# Perspectives on trust

“A base level of trustworthiness is required for our system to function. If we don’t have this then the system will break down. The economic costs of a breakdown of trust is catastrophic. Our economy, society and financial system cannot operate without trust.”

**Glenn Stevens, former Head of the Reserve Bank of Australia**

“People’s trust and confidence in our institutions and organisations provides the scaffold of society. Society could not function without this confidence.”

**Nev Power, COVID19 Recovery Commissioner**

“Laws only proscribe things. They don’t guide behaviour or tell you what to do – they just tell you what not to do. If there are no ethics, no inner compass, then you are left with a set of rules. Ethics and values inform most of our interactions with people across society.

Without ethics, there is an economic and social burden of enforcing rules-based frameworks to govern behaviour. Socially, the costs of policing rise. In markets, as Adam Smith identified, having a structure within which people trust one another means you can do deals on the basis of a handshake. Enforcement mechanisms impose a deadweight cost.”

**Ian Harper, Dean of Melbourne Business School**



“Trust is the compact that allows institutions in society to function, from family to the government. It is what binds society together.”

**Megan Motto, CEO Governance Institute of Australia**

“Ethics often occupies the space between acting in accordance with the letter of the law and acting within the intent of the law. While a compliance-driven culture can encourage people to act purely by the black-letter law, an ethical culture encourages individuals to think about the purpose of certain rules, and about the implications of their actions if they circumvent the purpose even where they remain compliant, including unintended effects on stakeholders. In the case of government, widespread discordance between the letter and intent of the law would likely stoke public distrust of government, thereby making policy more difficult to implement.”

**Grant Hehir, Auditor General of Australia**



Society's ethical infrastructure includes formal arrangements, such as: government regulators, integrity commissions, ombudsmen, and the judicial system. It also includes standards, guidelines and principles (such as the ASX Corporate Government Principles and Recommendations).<sup>13</sup> Within organisations, ethical infrastructure can include codes of conduct, whistleblowing systems, specific ethics committees/roles/codes/training, but also more general risk management systems, performance and reward systems, and hiring, promoting and firing policies. It can also include operational procedures for dealing with customer complaints, or for ensuring the quality of products or services. Across industries, ethical decision-making can be supported by professional codes of practice or industry bodies.

Ethical infrastructure also includes many informal elements, such as how unwritten conventions may guide the behaviour of a politician, or how a business leader's words and deeds might 'set the tone' for ethical culture within an organisation. Society also has many institutions that play an informal role in fostering ethical decision-making, including the media, education systems, NGOs, sporting bodies, faith groups and community organisations. Consumer activist groups, for example, may have societal goals in mind, but focus activities on specific businesses or organisations to drive corporate change.

There are limitations in trying to define and codify what ethical infrastructure is, because it is not just the items in the paragraphs above or what is listed in Table 2.1 – it is how the components fit together and individuals use them to inform their behaviour and ethical decisions. If a society or business just assembles the 'bones' of ethical infrastructure, without the muscle tissue that sits between components, it may still have weak ethical infrastructure. In fact, 'ticking the box' of ethical compliance may in fact do more harm than good if it provides a false sense that a society or business/organisation is ethical when reality is different.

A compliance-focused approach to ethics will have limited effectiveness because it can only drive behaviour that conforms to regulations or codes without fostering an intent to do what is right. In turn, this can dampen the critical faculties needed to recognise when systems, policies and structures become corrupted by unobserved 'mutations' in the underlying values and principles of an organisation (or society). On the other hand, it is a mistake to rely solely on informal approaches to ethical practice. In part, this is because of the natural variability in ethical literacy across society. In part it is due to the fact that some structure is always helpful in coordinating complex groups of people (e.g. in a large organisation).

Finally, we note that while businesses and other organisations often focus on how ethical infrastructure can be strengthened to support ethical decision-making, it is also important to recognise the institutional pressures on ethical behaviour. For example, remuneration structures might incentivise staff to act unethically towards customers. Team structures might reward collaboration and inadvertently encourage the sharing of sensitive information between staff. Organisations striving for strong ethical practice also need to be alive to such issues and make sure this part of ethical infrastructure is helping rather than working-against ethical decisions.

The key lesson here is that every formal system inevitably embeds and expresses underlying values and principles. In that sense, systems, structures, policies and their like are artefacts that both reflect and shape an organisation's culture. Thus, the ideal setting is one in which core values and principles are consciously expressed in an overall system that supports coherent ethical conduct without dampening the capacity for ongoing reflective practice.

Ethical infrastructure is as important for an economy as its physical and technical infrastructure; such as transport and communication networks. Strong formal institutions are seen as one of the fundamental drivers of long-run economic growth.<sup>15</sup> In the next chapter, we examine a way to quantify these economic and business benefits of stronger ethical infrastructure.

Table 2.1: Components of ethical infrastructure

## Society-level



### Formal/direct

- Judiciary
- Legislation
- Regulations
- Standards
- Guidelines and principles
- Professional bodies

### Informal/indirect

- Media
- Education system
- Faith groups
- NGOs
- Consumer activists
- Investor groups

## Businesses and organisations



### Formal/direct

- Codes of conduct/ethics
- Whistleblowing systems
- Training
- Risk management systems
- Performance reward systems
- Hiring, promoting and firing policies
- Ethics leaders
- Other business procedures

### Informal/indirect

- Leadership 'tone'
- Ethical role modelling
- 'Speak up' cultures
- Other behaviours

Source: Deloitte Access Economics (2020) and Harbridge, Gahan and Gentilin (2018)<sup>14</sup>

# Ethics and government

Maintaining high ethical standards within government is crucial to upholding trust in our democracy. Ethics is important for all institutions, but particularly for government given it makes laws, has great influence and is an ethical benchmark for society. As such, trust in government is a critical enabler of innovation – allowing a community to have confidence that it can risk embracing change while knowing that government will protect and preserve the public interest.

“Ethical decision making in government has a direct effect on trust in government, and this flows on to the effectiveness of public policy. If people don’t trust that public servants are making decisions in a balanced, fair and ethical manner, they are less likely to support policy.”

**Grant Hehir, Auditor General of Australia**

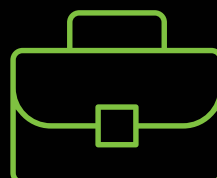
“Ethical decision making needs to be embedded in everything public servants and officials do. But this is often difficult. Public servants face complicated ethical decisions everyday, and it is often unclear what acting in the public’s ‘best interest’ means. Individual discretion is often necessary.”

**Michael Barnes, NSW Ombudsman**

Many of our consultees acknowledged that while ethical standards in government have improved over time, there is still a gap between public servants following the letter of the law and acting within the spirit of the law.

“The Public Service Act talks about ‘integrity, giving frank and fearless advice, avoiding conflicts’...As an auditor, we care not only about whether an entity is following the legal rules, but also whether it is acting within the intent of the law and community expectations.”

**Grant Hehir, Auditor General of Australia**





Grant Hehir outlined a list of ethical questions for government and public servants:

### **Procurement**

Are there enough entities in the tender process to ensure fair competition and to get the best value for taxpayers?

### **Withholding information**

Are you providing all relevant information to ministers, even if its not what they want to hear?

### **Avoiding parliamentary questions**

Are you answering questions openly and transparently, or avoiding, taking on notice or just partly answering?

### **Probity rules**

Are you actively managing conflicts of interest, or just declaring them?

While these actions rarely amount to actual corruption, there is a disconnect between acting within the letter and intent of the law. Grant Hehir believed this was due to cultural problems, not dissimilar to cultural issues facing many other organisations, and that "in order to have an ethical organisation, you need to have ultra-ethical leaders."



# Ethics in journalism

The media plays an important role within society's ethical infrastructure. It shapes public debate, and holds people and institutions to account. Because of this power, ethical standards within the media are vital. Deloitte Access Economics spoke to investigative journalist, Kate McClymont, about the media's role in maintaining ethics in our democracy, as well as the role of ethics within the media industry itself.

**"The media wields a lot of power, and with this comes responsibility, moral choices, ethical dilemmas. Every story has these choices. We often make mistakes but when we do so its important to acknowledge and correct the record as quickly as possible."**

Ethical standards, within journalism, play a crucial role in preserving public trust in reporting. Research suggests that trust in news media is declining in Australia, with perceptions of bias and conflicts of interest the biggest factors undermining trust in news.<sup>16</sup> McClymont pointed to increasing commercial pressures and the rise of new online media as factors leading to this decline.

**"Commercial pressures are meaning that the moral foundations of some sections of the media are being eroded. The fracturing of the media in these sections is in turn fracturing moral and ethical decision making. This is a chicken and egg scenario; journalists don't have the time and resources to do their job properly, and consequently people are less informed and more distrustful of the media."**

McClymont outlined how traditional newsrooms had more time to understand stories and properly convey nuance in their reporting. The rise of new online media and the decline of traditional newsrooms has resulted in the 'rush to be first' where 'gotcha' moments prevail. Issues are rarely black or white, but consumers of new media don't want grey. These pressures are driving sensationalised reporting with less nuance, fairness and accuracy, leading to more polarised opinions in society.

**"The media is of society and we reflect society. In general, we could do our job a lot better if we had more time, if there weren't commercial pressures to have gotcha moments. The rush to be first in online media is eroding nuance and dividing democracy."**

Key questions for journalists to consider when writing stories:

- Is the story fair and accurate with information put into proper context?
- Have you thought about any unintended consequences of a story?
- Have you treated sources fairly and have you spoken to enough people?
- Is the story in the public interest?



# Indigenous Australian Perspectives on Ethics

Contributed by members of Deloitte's Indigenous Leadership Team, Worimi man Deen Sanders and Kamillaroi man Rick Shaw

Ethics is often framed in the Western traditions as an enlightened way of thinking. That is, different from 'normal' thinking and something that challenges or layers over the top of 'normal' ways of living. This is because so much of the Western perspective on society, psychology and even economics begins with the singular unit of 'self' and the maximisation of that self. This is why Western approaches often present ethics as a correction of that self, as a restraint against self interest.

An indigenous perspective begins outside the self, and sees all activity as serving the purpose of creating abundance and harmony for all. For us, ethics is wrapped into the core of our being, because we see ourselves as custodians of the land from which all benefit. The interests of the land are inseparable from the interests of its people. The ethics of the system are the intrinsic aim of the system, not an externally imposed restraint on commercial or other outcomes. Our cultures measure knowledge and shared outcomes, not individual accumulation. We revere wisdom, not wealth.

This is not an eschewing of the self but a clear recognition that the interests of the self are the same thing as the interests (collectively and intergenerationally) of the land and the people. The self is activated by its responsibility to that whole and to each other.

Sayings like "If you don't move with the land, the land will move you" are not quaint euphemisms, they are statements of geographic, cultural and economic fact with many layers of truth and meaning. They are an ethos in themselves, spoken through the land. For us, acting with integrity is acting in alignment with the land, which in turn provides an infinitely bountiful gift. We offer a way of looking at the world where the value of living ethically far exceeds \$45 billion or any artfully constructed price tag.

Australian Aboriginal culture is continuous and thriving, our cultures are reviving, old ceremonies are being resurrected and revitalised. We are emerging from the shock of the last 200 years. Guided by the Uluru Statement from the Heart, First Nations people are looking to take our rightful place in Australia's future. For us, we are meeting non-indigenous Australians as if for the first time, and this time our eyes are open.

The mindset of colonisation comes from and continues to be part of the Western ethical framework. The Western ethical frameworks which gave rise to and justify colonisation remain intact, even if there has been some modification of what is acceptable behaviour. There are inherent limitations in axiomatic ethical frameworks. These frameworks set up dualistic binaries (centre/periphery, self/other, white/black) which are alien to us. This report considers only Western ethical frameworks because current applied tools of measurement, and the applied tools of political and social construction, cannot be separated from a Western mindset. In a postcolonial world, an Indigenous ethical perspective means Australia can be better than this, for everyone's interest.

The colony of Australia is founded on dispossession based on a construct of land as capital, morally justified by denigrating and othering the original peoples. The inability to truly acknowledge past wrongs and to embrace Aboriginal culture stains the hearts of non-Indigenous Australians and undermines the efficacy and utility of the ethical frameworks we try to apply from other lands. Those rules-based ethical frameworks have guided the practices of church, state and corporations to abuse power and act in ways that have led to a proliferation of Royal Commissions. The challenge and opportunity for Australia is to reform its legal, moral and social codes and build out from Indigenous ways.

We have a great desire to share Indigenous lore to encourage living in harmony with the land. Even with the best intentions, those from outside Indigenous culture must be wary of appropriation. As is the way with all true knowledge, it cannot be taken or claimed. It doesn't live in treatise or textbooks and resists pithy summary. It is taught, experienced and earned. Claiming of knowledge without grasping the many depths underlying Indigenous lore is more than swimming on the surface of a vast ocean, it can cause deep practical and spiritual harm. The country is alive with lore and it sits uncomfortably beneath the feet of those unable or unwilling to properly connect to it. We want that connection for everyone, and it is available for those who seek it.

That truthful connection begins with an awareness that an Indigenous perspective of ethics and knowledge has safely sustained and supported the oldest, continuous culture on the planet. An Indigenous framing of ethical life was the right perspective for this country for the many tens of thousands of years before the creation of Western ethical frameworks and it remains true forever for this country. A proper embracing of it will guarantee a new and extraordinary future for all Australians. A superficial appropriation will do more harm than good. A patina of acknowledgement cannot substitute for substantive embrace of a culture. The challenge for Australia is to embrace Indigenous ways as central to our concept of nationhood, not to wear it as a badge to cover the nation's shame.







When white settlers first started exploring inland Australia, they heard stories of a large snake moving through the country, shaping the land. They dismissed these stories as the myths of a stone age people. Actually, they were being told where to find water.

# 3. Ethics and the economy

## 3.1 Ethical behaviour and the economy: a framework

Ethics can have significant economic and social impacts. For individuals, ethics can affect mental and physical health and job outcomes; at the business level, they affect relationships with customers and staff, productivity, profitability; and, across the economy, they have a significant impact on levels of compliance costs, the functioning of markets and ultimately, living standards. Figure 3.1 sets out a framework for considering the different levels at which ethics and ethical infrastructure can impact the economy.

**Figure 3.1: The economic and social impacts of ethical behaviour and infrastructure**

<b>Ethics &amp; ethical infrastructure</b>	 <b>Level</b>	 <b>Individual</b>	 <b>Business</b>	 <b>Economy</b>
	 <b>Impacts</b>	Reduced moral injury Increased trust/ social capital	Strong stakeholder relationships Higher public trust	Reduced friction and smoother functioning of markets Higher trust and social capital
	 <b>Measures</b>	Mental & physical health Labour market participation	Productivity, profitability, brand metrics Reduced compliance costs	Higher economic growth Lower regulatory & compliance costs

Source: Deloitte Access Economics (2020)

# Ethics and economics – in conflict or in harmony?

At a superficial level, ethics and economics might seem to be in tension. A common caricature of economics is that it conceives of society as no more than a group of self-interested individuals maximising their own utility with little genuine concern for others. On this view, economics might seem fairly hostile, or at least apathetic, to ethics. While there are obviously cases of conflict between the individual and the common good, a deeper inspection reveals a strong, positive relationship between ethics and economic prosperity.

Since the time of Adam Smith, ethics has in fact been embedded in the study of economics. Smith, who was a moral philosopher who pioneered the subject of modern economics, himself stated in *The Theory of Moral Sentiments* (1759) that:

*“How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others, and render their happiness necessary to him, though he derives nothing from it except the pleasure of seeing it.”*

For Smith, acting in one’s self-interest could benefit society (albeit unintentionally) as a whole as if by an “invisible hand”, but acting ethically and being interested in the “fortune of others” could play a role in one’s decisions too. Smith also recognised that markets would not always produce socially beneficial outcomes and was a critic of the slave trade.

Behavioural economics has since shown this to be true. When people make economic decisions, they do not only consider self-interest, they also take into account ethical considerations and the effect of their choices on others. Firms similarly do not only consider profit maximisation in making business decisions. Ethical standards, corporate social responsibility and the long-term costs of unethical conduct to reputation and stakeholders also play a role in decision-making. Markets do not only operate on competition and profit motives – institutional economics has shown that an economy critically also needs cooperation, trust, and confidence to function smoothly.

Ethics is much more in harmony with economics than at first glance and as Amartya Sen, a Nobel Prize-winning economist, once put it economics could “be substantially enriched by paying more attention to ethics”, just as the study of ethics would also “benefit from a closer contact with economics”.



### 3.1.1 Individual outcomes

Ethical behaviour and infrastructure have been found to be positively associated with a range of individual outcomes ranging from improvements to mental and physical health to improved labour market outcomes.

The link between ethical behaviour and **improvement in health outcomes** can occur both directly and indirectly. People, who engage in ethical behaviour, are less likely to experience mental stress and trauma associated with breaching their own personal ethical standards ('moral injury'). They are also less likely to resort to poor health behaviours, such as smoking, alcohol consumption and reduced exercise, as a coping mechanism after committing unethical acts.<sup>17</sup> Similarly, people who perceive or witness less unethical behaviour around them, are also less likely to suffer from secondary mental stress or engage in negative health behaviours to overcome the unethical conduct of others.<sup>18</sup> In both cases, this can lead to better individual mental and physical health outcomes, as well as higher levels of general wellbeing.<sup>19</sup>

A number of empirical studies have confirmed this relationship. Using data from the Household, Income and Labour Dynamics in Australia (HILDA) survey, Levula, Wilson and Harré (2016) find that perceived ethical behaviour and trust within a community are statistically significant determinants of an individual's mental health scores across all life stages.<sup>20</sup>

They observe that in adults, a unit increase in perceived ethical behaviour and trust scores measured between 0 and 18 is associated with a 1.3 unit increase in individual mental health scores measured between 0 and 100.<sup>21</sup> This effect was significant, but less pronounced, in other life stages – in adolescents, a unit increase in perceived ethical behaviour and trust scores was associated with a 1.0 unit increase in mental health scores and a 0.4 unit increase for seniors.<sup>22</sup> Berry and Welsh (2009) follow a similar approach and find that perceived ethical conduct in a community is not only an important determinant of individual mental health scores but also physical and general health scores in the HILDA survey.<sup>23</sup>

Ethical behaviour can also play a role in helping people to participate in the labour market. In particular, they can improve norms of reciprocity and interpersonal trust, adding to the stock of 'social capital'<sup>24</sup> within a community.<sup>25</sup> Social capital can, in turn, reduce job search frictions and information asymmetries between employers and potential job applicants in the labour market.<sup>26</sup> Employers are able to trust their employees to do the 'right thing', helping to overcome the principal-agent problem and to facilitate higher labour market participation rates for individuals within a community.

### 3.1.2 Business outcomes

Ethical behaviour and infrastructure are also potentially associated with better financial outcomes for businesses. This link has mainly been explored in the context of the corporate social responsibility literature. Firms, which act ethically and have ethical infrastructure in place, are likely to enjoy improved relationship with their stakeholders and are able to build a greater trust with the broader public. This can manifest in reduced production costs from improved supplier relations, increased work engagement from positive employee relations, lower compliance and administration costs from better government relations, and higher sales from stronger customer relations.<sup>27</sup> Firms can thus potentially experience greater operational efficiency, productivity and profitability from acting ethically and having ethical infrastructure.<sup>28</sup>

The empirical relationship between corporate social responsibility and business performance can be difficult to untangle given that causality can run both ways. One study which found a positive impact between corporate social responsibility and financial performance is Eccles, Ioannou and Serafeim (2012), who consider the effect of sustainability policies on long-term financial performance.<sup>29</sup> Comparing corporations, which voluntarily adopt sustainability policies ('high sustainability companies'), with those that do not ('low sustainability companies'), they find that annual abnormal return performance is higher for the High Sustainability group compared to the Low Sustainability group by between 2.3% to 4.8%.<sup>30</sup> They further find that high sustainability firms also perform better when looking at accounting rates of return, such as return-on-equity (ROE) and return-on-assets (ROA).<sup>31</sup>

# Ethical decision making and moral injury

Moral injury describes the psychological effects of betraying one's values, principles or deeply held beliefs. These effects can include feelings of shame, guilt, disgust and rumination, and it is these patterns of thinking that lead to burn out, fatigue and mental illnesses like PTSD. Psychiatrist, Jonathan Shay, describes moral injury as "the soul wound inflicted by doing something that violates one's own ethics, ideals, or attachments".<sup>32</sup>

Moral injury can occur in all contexts, but people are particularly at risk when they are making decisions that have deep and long term consequences for others. While the term was first ascribed to war veterans suffering PTSD, it has more recently been applied to situations during COVID-19, such as health care workers having to make triage decisions, or business leaders deciding to fire employees or reduce pay.

Robust ethical decision making is crucial in these moments, both during the decision, and afterwards when communicating the decision to others. During the decision, individuals with developed ethical literacy skills will be better able to analyse the morally important features of the situation, and weigh these up accordingly. This includes reflection on potential consequences, what duties they have, and how the action would reflect on their personal or organisation's character. Structured reflection through an ethical decision making framework helps exercise our 'moral imagination' – understanding other people's values, beliefs and motivations – and avoids acting from the 'lash of necessity', thereby decreasing the chances of moral injury.





More recently, Cornell and Damadoran (2020) review the literature and note that while the relationship between corporate social responsibility and profitability appears positive it is sensitive to the way corporate social responsibility and profits are defined. While they question whether the relationship between improved corporate social responsibility and profits is truly causal, they do note there is evidence that companies that act negatively (i.e. clearly unethically) have poorer financial outcomes.<sup>33</sup>

Engaging in ethical conduct and having strong ethical infrastructure can also potentially improve the share market performance of a business, particularly in the form of reduced price volatility during negative market shocks. Lins, Servaes and Tamayo (2017) find that firms with high social capital experienced stock returns between 4 to 7 percentage points higher than firms with low social capital – even during the 2008 Global Financial Crisis.<sup>34</sup> Stubben and Welch (2020) take a slightly different approach and adopt use of company internal hotline reporting systems as a proxy measure for ethical behaviour.<sup>35</sup> They find that increased use of internal hotline reporting systems at a company is associated with greater profitability and workforce productivity as measured by Return on Assets (ROA).<sup>36</sup>

### 3.1.3 Economy-wide outcomes

Across an economy, the behaviour of individuals and businesses, together with well-established ethical infrastructure, can lead to increased levels of trust and confidence in all sectors. The key to increasing trust is to ensure that behaviour aligns with expectations. This is achieved when an individual or an organisation publicly declare the basis on which they will act (their values and principles) and then act accordingly. Strong alignment with socially constructive values and principles – that is, ethical conduct – builds trust. Higher levels of trust can, in turn, help smoothen the functioning of markets and **reduce the costs of regulation**, resulting in **greater economic growth** and **increased levels of wellbeing**.

A number of empirical studies from the institutional economics literature have explored this relationship between ethical behaviour and infrastructure, trust and economic growth. Erdem and Tugcu (2011), for example, consider the relationship between the ethical behaviour of businesses and economic growth.<sup>37</sup> Using the number of bounced cheques and protested bonds as a proxy for the degradation of business ethics, they find that business ethics is a statistically significant determinant of economic growth and that the degradation of it negatively affects long-term growth rates for Turkey.<sup>38</sup> Ng, Ibrahim and Mirakhor (2015) consider the dynamics of the relationship more closely, looking at business ethics, trust, stock market development and economic growth. They observe that the relationship between stock market development and economic growth is only significant and positive, after the attainment of a certain threshold level of business ethical behaviour and trustworthiness.<sup>39</sup> That is, a minimum level of ethical behaviour and trust appears to be required before markets are able to function smoothly and contribute positively to economic growth.

More broadly, Knack and Keefer (1997), as well as Guiso et al. (2006), Tabellini (2008) and Algan and Cahuc (2010), have confirmed the positive relationship between trust and economic growth across countries.<sup>40</sup> These findings are discussed in greater detail in section 3.2 below.

Other studies in the literature have looked instead at the relationship between ethics and more formal regulation in an economy. Viewed as a set of moral norms, ethical behaviour and infrastructure can act as a partial substitute for more formal regulation in an economy. Ethical behaviour can reduce the need for more costly formal regulation and compliance activities.

Deloitte Access Economics (2014) has previously estimated the costs of government red tape and found that public sector regulation burdened the Australian economy at a cost of \$94 billion a year.<sup>41</sup> This included both the cost to taxpayers of creating, administering and enforcing public sector regulation, as well as the cost to individuals, business and the public sector of complying with public sector regulation.

# Ethics and the finance industry

The 2019 Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry highlighted a multitude of ethical failings. This has resulted in the imposition of an estimated \$2.4 billion in compliance costs, fines and customer remediation for the Big Four Banks alone.

Some of the worst practices included: levying fees for no service, charging dead people, accepting bribes, facilitating addictions of problem gamblers, and encouraging people to take on high risk products unsuited to their needs. While the finance sector may have benefitted in the short term from some of these practices, the longer term fall out and costs associated with customer remediation has been significant – in part reflected through significant declines in share prices for the major banks.

We spoke to Glenn Stevens, former Governor of the RBA, who commented on the importance of moral courage and conviction, as well as owning up to one's mistakes.

"All institutions have a job or purpose. Individuals within institutions must ask 'what is the right thing to do?' then have the courage to act on these convictions, even if its not popular."

**Glenn Stevens**

Ian Harper, Dean of Melbourne Business School, argues that 'sunlight' that is shone and exposes ethical failings is crucial in improving standards. While moral fortitude and courage are important, often it is the fear of punishment and reputational damage that motivates people to do the right thing. Harper spoke about common psychological drivers of ethical failure.

"Three common sources of ethical failure or temptation are ambition, approbation and appetite. Ambition is being self-interested and putting your own interests ahead of others; approbation is glory-seeking and looking out for things that will give you praise; appetite is manipulating circumstances to satisfy your desires."

**Ian Harper**

While the most egregious findings from the Royal Commission were arguably unlawful, many of Kenneth Hayne's recommendations were not about issues of law-breaking behaviour per se. Instead, they were linked to unethical cultures where staff acted unethically. As is the case in other industries, this can be understood as people not acting within the spirit of the law. As such, there has been a call for greater professionalisation of the finance industry. 'Professionalising' an industry includes measures such as setting up an oversight body and governing ethical framework that, amongst other things, establishes overriding duties owed to customers. Such an approach can be seen in the Commonwealth Government's establishment of the Financial Advisers, Standards and Ethics Authority (FASEA) and the enshrinement, in law, of its Code of Ethics by way of Legislative Instrument.



# Ethics and the costs of corruption

Ethical behaviour and infrastructure can also play an important role in reducing corruption and minimising the costs of corruption on the economy. While it has been argued, in some quarters, that corruption might 'grease the wheels' and provide short-term gains to an economy from avoiding the costs of bureaucratic rules and regulations, research has consistently shown that corruption does not come without costs and can negatively affect the longer-term growth of an economy.<sup>42</sup>

Around the world, the total economic cost of corruption has been estimated by the World Economic Forum to be worth \$3.6 trillion a year or about 5% of total global gross domestic product (GDP).<sup>43</sup> This figure only includes bribes and stolen money and does not include the many other forms of corruption such as money laundering, tax evasion and cronyism. In Australia, corruption has been similarly estimated to cost about 4% of national GDP or just over \$72 billion a year.<sup>44</sup>

Corruption can also restrain a countries' growth in the longer term. Mo (2001) shows that a 1% increase in corruption levels, as measured by the Transparency International Corruption Perception Index, reduces a country's economic growth rate by as much as 0.72%, through increasing political instability and reducing the level of human capital and private investment.<sup>45</sup> Dreher and Herzfeld (2005) similarly find that a 1 index point increase in the Transparency International Corruption Perception Index decreases a country's economic growth rate by 0.13 percentage points or about \$US425 in GDP per capita terms.<sup>46</sup>



# Ethics and the environment

Addressing climate changes is arguably the largest collective challenge that humanity has ever faced. This is not the only issue within the scope of environmental ethics, but it is one with great consequence. As Mara Bun, President of the Australian Conservation Foundation noted, climate change is a complex ethical issue that individuals can act on, but which will ultimately require broader behaviour change.

“One of the biggest ethical challenges of our times is confronting the cognitive dissonance that exists between our existing modes of living, and future economic growth. Our current economic system is not equipped to tackle climate change seriously.”

**Mara Bun, President of the Australian Conservation Foundation**

Mara pointed to alternative models such as ‘Doughnut Economics’ where social indicators like food security, health and education (inspired by the Sustainable Development Goals) are balanced with ecological indicators like climate change, land conservation and biodiversity loss.

Mara also highlighted how technology can aid sustainability outcomes. For instance, Microsoft is a now world leader in sustainability, committing to be carbon negative by 2030, with the objective of removing all of the carbon it has emitted since it was founded in 1975 by 2050.

The rise of ‘ethical investing’ evidences a growing awareness of environmental and social concerns. Driven by shareholders demanding greater transparency over their investments, many funds now assess their portfolios for Environmental, Social or Governance (ESG) risks, or refuse to invest in specific industries, such as tobacco or armaments.

As Mara outlined, there are various initiatives that inspire hope in our response to climate change, and understanding the interplay between individual and societal-level responses is a key focus for environmental ethics.



# Ethics and law enforcement

As recent Black Lives Matter protests around the world demonstrate, the relationship between law enforcement and the community is crucial in maintaining harmony and social cohesion.

Deloitte Access Economics consulted with Andrew Scipione, the former Commissioner of the New South Wales Police Force, who discussed the importance of a collaborative approach to policing. Police should be the “custodians of the community”, and the community’s best interest should be at the core of any law enforcement initiative.

“Trust is the basis of respect, which is the basis of police service. The moment you can’t trust, you can’t respect, you can’t serve.”

**Andrew Scipione**

Scipione highlighted a number of measures that have improved police professionalism, such as requiring a university qualification, making clearer the expectations from leadership and the community, and tools and training to be able to more effectively deal with difficult situations.

“NSW has only 20,000 police officers with 6 million people. When there is trust between police and community, crime decreases massively as people are more likely to report suspicious behaviour. They act as eyes and ears for the police.”

**Andrew Scipione**

As well as the economic cost of crime, there is also a large social cost. Crime has the potential to substantially impact victims’ psyche, including feeling unsafe and increased pessimism and general anxiety.

Bureau of Crime statistics show that crime has decreased over 17 categories from 2005 to now. Scipione argued that the drop in violent and property crime is linked to increasing professionalism.







## 3.2 Economic modelling

The previous section outlined the substantial body of research on the economic and social impacts of ethics at both the individual and business level. When individuals act more ethically, they are more likely to experience better labour market and health outcomes and when businesses act more ethically they are likely to achieve improved financial outcomes, in the long term.

In this section, economic modelling is undertaken to examine the degree to which ethical behaviour can improve labour market and health outcomes for individuals. The subsequent sections look at the impact of ethical behaviour on business performance before considering how trust, built through the mutual and collective ethical behaviour of individuals and businesses, might lead to improved economic growth and development for Australia.

### 3.2.1 Individual impacts

#### 3.2.1.1 Data used in the analysis

To examine the role of ethical behaviour on labour market and health outcomes at the individual level, we again draw on data from the HILDA survey (which was discussed in Chapter 1). HILDA is Australia's first nationally-representative household-based survey and is funded by the Australian Government through the Department of Social Services. It has followed more than 17,000 individuals since 2001, collecting detailed data on their employment status, income, education, housing, health and wellbeing.

In addition to those indicators, HILDA also collects data on more personal aspects of individuals' lives, from their relationships, attitudes and values, to major life events. The HILDA Self-Completion Questionnaire (SCQ) contains a range of subjective questions, asking respondents the extent to which they agree with certain statements about society such as "Generally speaking, most people can be trusted" or, "Most of the time people try to be helpful". Respondents can score their level of agreement with a statement between 1 and 7, where 1 indicates that they "strongly disagree" with the statement and 7 indicates that they "strongly agree".

Most relevantly, the HILDA SCQ contains questions about perceptions of ethical behaviour in society. Across 5 waves of the survey, respondents are asked about their level of agreement with the three following statements:

1. Most people you meet keep their word;
2. Most people you meet make agreements honestly; and
3. Most people you meet succeed by stepping on other people.

While these statements may not be exhaustive of all the different types of observable ethical/unethical behaviour in society, they do capture a number of critical behaviours and provide a reasonable indicator of the degree to which an individual perceives ethical behaviour to be present in the people around them.

To obtain a measure of ethical behaviour in Australia, we construct an individual and a region-based ethical behaviour index using responses to these three statements. We first reverse code responses to the third statement, so that higher scores correspond to a stronger individual perception that most people do not step on other people to succeed. All statement responses are then adjusted from a scale of 1 to 7 to a scale of 0 to 6 and summed to derive an individual-based ethical behaviour perception index measured between 0 and 18. This is similar to the approach taken by both Levula, Wilson and Harré (2016) and Berry and Welsh (2009).<sup>47</sup>

Table 3.1 provides some summary statistics of our individual ethical behaviour index.

This individual-based index importantly provides a measure of the degree to which a person perceives positive ethical behaviours to be present in the people around them. In line with past studies showing how an individual's perceptions of ethical behaviour in others can impact their own mental and physical health,<sup>48</sup> we use this individual ethical behaviour perception index when modelling the relationship between ethical behaviour and individual health outcomes.



**Table 3.1: Summary statistics for our individual ethical behaviour index**

	Observations	Mean	Standard deviation	Min	Max
Individual ethical behaviour perception index	64,802	11.7	3.4	0	18
• Most people you meet keep their word	65,135	3.7	1.4	0	6
• Most people you meet make agreements honestly	65,079	4.0	1.3	0	6
• Most people you meet do not step on other people to succeed*	65,009	4.0	1.5	0	6

Source: HILDA (2020); Deloitte Access Economics (2020) modelling.

Note: \*This variable is constructed by reverse coding the “Most people you meet succeed by stepping on other people” variable in the HILDA SCQ, so that higher scores correspond to a stronger individual perception that most people do not step on other people to succeed.

In looking at the relationship between ethical behaviour and individual labour market outcomes, we adopt a slightly different measure of ethical behaviour, which is region-based. This is because past research has shown that the primary mechanism by which ethical behaviour is able to affect individual labour market outcomes is by feeding into the wider stock of ‘social capital’ within a community or a region. In other words, it is the actual or perceived ethical behaviour in a region which can have an impact on the labour market outcomes of individuals located in that region. We therefore group the above individual ethical behaviour scores by regions and by years to consider a region’s perception of its own ethical behaviour in a given year. Mean ethical behaviour scores are produced for the different regions – 13 Greater Capital City Statistical Areas (GCCSAs) – for each year of available data and assigned to individuals residing in each region to create a regional ethical behaviour index. This, importantly, means that our regional ethical behaviour index measures a region’s perception of ethical behaviour in a given year and varies across individuals, depending on which region they are located in. In doing so, our index provides a measure of the degree to which there is perceived ethical behaviour within a region in a given year.

Table 3.2 provides summary statistics of our regional ethical behaviour index.

In addition to the regional ethical behaviour index, based on the three questions outlined above, respondents were also asked in six HILDA waves the extent to which they agreed with the following statement:

**Most people would try to take advantage of you if they got a chance.**

As a further robustness test, the analysis was also undertaken using responses to this question (labelled individual perceptions of advantageous behaviour). The results were broadly similar, indeed slightly stronger than for the regional ethical behaviour index. The results based on this alternative measure of ethical behaviour are set out in detail in Appendix A.

**Table 3.2: Summary statistics for our regional ethical behaviour index**

	Observations	Mean	Min	Max	Max
Regional ethical behaviour index	98,980	11.7	8.0	12.6	18

Source: HILDA (2020); Deloitte Access Economics (2020) modelling.



### 3.2.1.2 Modelling approach

To examine the relationship between ethical behaviour and employment and health outcomes, Deloitte Access Economics used a form of statistical analysis known as regression analysis. The purpose of this analysis is to examine the strength of the relationship between ethical behaviour and individual employment and health outcomes, after controlling for a range of other characteristics that may impact employment and health.

Our control variables included an individual's age, gender, their highest educational qualifications, marital status, whether or not they had children and the educational qualifications of their parents. In our analysis of the impact of individual perceptions of ethical behaviour on individual health outcomes, we added employment status as a further control. In our analysis of the impact of regional ethical behaviour on individual employment outcomes, we additionally controlled for years of work experience (a common control variable in the labour economics literature) and restricted the sample to those aged between 21 and 65 to capture individuals that are most likely to be in the labour force.

A range of different model specifications were then used to estimate the relationship between ethical behaviour and individual employment and health outcomes. This importantly allowed us to consider how sensitive our results were to different functional forms and to check the robustness of our results.

The results of these different models are set out in further detail in Appendix A.

### 3.2.1.3 The relationship between ethical behaviour and individual health outcomes

In considering the relationship between ethical behaviour and health outcomes, we looked at individual mental, physical and general health outcomes and applied regression analysis to examine how perceptions of ethical behaviour affected an individual's health outcomes.

The HILDA questionnaire contains 36 questions based on the Medical Outcomes Study Short Form (SF36), a widely used approach to measuring self-reported individual health status. These 36 items can be combined to generate eight different health concepts: physical functioning, role physical, bodily pain, general health, vitality, social functioning, role emotional and mental health, each drawing on multiple items in the survey. The analysis of health outcomes is focused on three of these eight concepts, namely:

- Mental Health,
- Physical Functioning, and
- General Health.

Each of these concepts is calculated based on responses to a number of questions and standardised so that they are reported on a scale of 0 to 100.

From the results of our regression analysis, Deloitte Access Economics found that perceptions of ethical behaviour was both a positive and statistically significant determinant of an individual's health outcomes, even after controlling for other factors that could affect those health outcomes.

This was the case across all health outcomes considered – mental, physical and general. In particular, a one unit increase in our individual ethical behaviour perception index (measured on a 0 to 18 scale) was associated with:

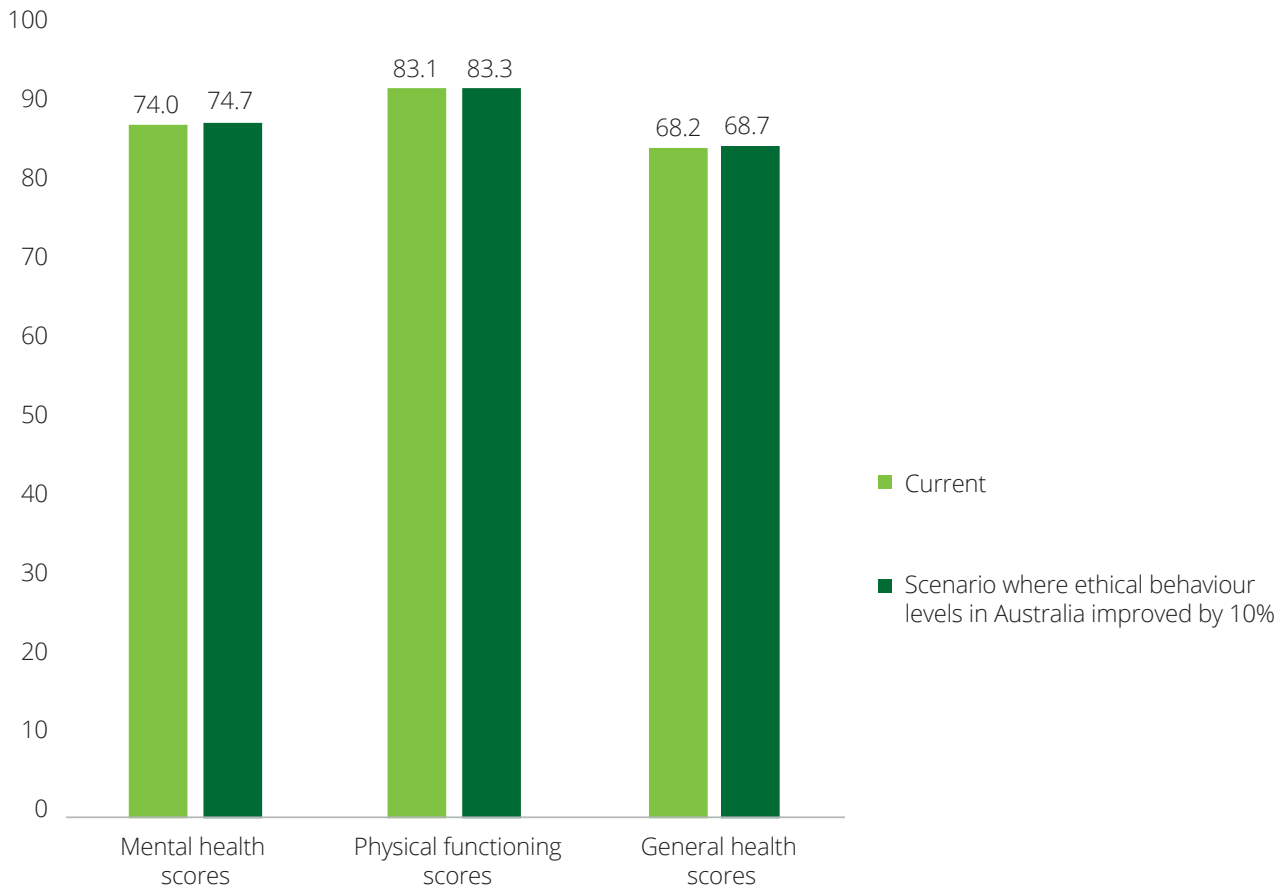
- a 0.6 unit improvement in Mental Health scores,
- a 0.1 unit increase in Physical Functioning scores, and
- a 0.4 unit rise in General Health scores (all measured on a 0 to 100 scale).

To illustrate what this finding means in terms of how a more ethical society might improve employment in Australia, we considered a scenario in which ethical behaviour levels in Australia increased by 10%. In such a scenario, the average person would see their:

- Mental Health score improve by 0.7 units from 74.0 to 74.7 units,
- Physical Functioning score increase by 0.2 units from 83.1 to 83.3 units, and
- General Health score increase by 0.5 units from 68.2 to 68.7 units.

Chart 3.1 illustrates these results where the ethical behaviour levels in Australia were to rise by 10%.

**Chart 3.1: The impact of improving ethical behaviour in Australia on individual health outcomes**



Source: Deloitte Access Economics (2020) modelling; HILDA data.

**3.2.1.4 The relationship between ethical behaviour and individual labour market outcomes**

In considering the relationship between ethical behaviour and labour market outcomes, Deloitte Access Economics applied regression analysis to examine how ethical behaviour within a region affected an individual's probability of being employed and their wage level.

The results of the analysis in relation to employment were mixed. There was no statistically significant relationship between the regional ethical behaviour index and individual employment outcomes. However, there was a positive and statistically significant relationship between the alternative measure of individual perceptions of advantageous behaviour at a regional level. This suggests that the relationship between regional ethical behaviour and individual employment remains unclear. It is possible that because measures of ethical behaviour are only recorded in five waves, and an individual's employment status does not typically change much from year to year, it may be difficult to precisely determine the relationship between ethical behaviour and employment status using the HILDA data.



The analysis also examined the impact of changes in the regional ethical behaviour index on wages. These results showed that a one unit increase in the ethical behaviour index was associated with a statistically significant increase in real wages of between 2.3% to 5.7%. A 10% increase in regional measures of ethical behaviour would be associated with an increase of 2.7% to 6.6% in individual wages across the models considered. On an economy wide basis, a 2.7% increase in wages equates to an aggregate wage increase of almost \$23 billion.

### 3.2.2 Business modelling

Acting ethically has also been linked to better financial outcomes for some businesses. To investigate the link between the perception of a firm's ethical behaviour and their financial outcomes, we draw on data from the RepTrak Company's Reputation Index. Since 2008, the Reputation Index has surveyed over 10,000 Australians each year and asked for their perceptions on the reputation of 60 of Australia's largest companies, by revenue.<sup>49</sup> The index asks Australians for their views on whether a company has a good overall reputation, whether they have a good feeling about the company, whether the company is one they trust and a company they admire and respect. Responses to these questions are then aggregated to produce the index's annual reputation or 'Pulse scores' for each company.

In addition to these reputation scores, the index also asks Australians to consider the performance of these companies across the seven following reputation drivers:

1. Products and Services
2. Innovation
3. Workplace
4. Governance
5. Citizenship
6. Leadership, and
7. Performance.

Most relevantly, the Governance driver looks at whether a company is a responsibly-run company, which behaves ethically and is open and transparent in its business dealings. Respondents are specifically asked to score businesses based on their performance in:

- How fair in business they are,
- How ethically they conduct their activities and
- The degree to which they are open and transparent.

These Governance scores, which are measured on a scale of 0 to 100, importantly provide an indicator of the degree to which a company is perceived to be ethical. To obtain a measure of the perception of a firm's ethics, we therefore use the Governance scores from the RepTrak Company's Reputation Index over the period 2009-2020. We then match the index to annual financial performance data from IBISWorld. The outcome considered was a firm's Return on Asset (RoA).<sup>50</sup>

The modelling takes into account a number of factors to ensure a precise effect of a firm's ethical perception on financial outcomes is estimated. These factors include taking into account a firm's financial performance in the previous year (which tends to be highly correlated with its performance in the future) as well as taking into account idiosyncratic firm, industry and year characteristics which are also likely to impact financial performance. The econometric modelling equation is set out below:

$$RoA_{i,t} = Governance\ score_{i,t} + RoA_{i,t-1} + a_i + IND_i + u_t + \varepsilon_{i,t} \quad (1)$$

where firm  $i$ 's ROA in year  $t$  is a function of its ROA in the last period (i.e. year  $t-1$ ), its Governance score in year  $t$ ,  $a_i$  is a time-invariant company variable capturing company fixed effects,  $IND_i$  is a set of industry controls,  $u_t$  captures year fixed effects to account for differences in economic conditions by year and  $\varepsilon_{i,t}$  a normally distributed error term.



Table 3.4 presents select results from the business performance modelling. Moving up one point in RepTrak's Governance index leads to a 1% increase in return on assets, a result which is statistically significant at the 10% level or weakly significant. Given the average return on assets is 13% this implies that a one unit increase in Governance scores can lead to a 7.6 percent increase in a firm's return on asset. If a firm is able to improve their Governance score by one standard deviation (approximately 7 points), they would expect to see an increase of over 50 percent in their Return on Assets. However, it is worth noting that this relationship was only significant at the 10% level. Further research could look to examine this relationship with a larger sample of firms. Similarly, the modelling indicated that improving a firm's pulse score, which includes governance as part of a range of measures, also lead to an improvement in return on assets, which was statistically significant at the 1% level. Further details of the modelling and results for the broader Pulse Index are set out in Appendix B.

These results provide some further evidence that there is a business case for business' improving ethics. In addition to the moral reasons for businesses to become more ethical, there is also evidence that being ethical can be associated with improved financial outcomes for businesses.

### 3.2.3 Trust and income across countries

There has been a considerable amount of recent research addressing the links between institutions and culture on economic growth and development. Within this broad research theme, the role of trust on growth has been a topic of particular interest. Research on the importance of trust and its role in economic activity tends to stem from Arrow (1972) who stated, "Virtually every commercial transaction has within itself an element of trust, certainly any transaction conducted over a period of time. It can be plausibly argued that much of the economic backwardness in the world can be explained by the lack of mutual confidence".

The economic gains of trust arise from the fact that it favours cooperative behaviour and thus facilitates mutually advantageous exchange. Economic activities that require individuals to rely on the future actions of others are conducted at a lower cost in high-trust environments. These transactions are the building blocks of an economy. Examples of such transactions include the exchange of products for future payment, employment contracts as well as all investment and savings decisions.

High trust societies are characterised by norms of civic cooperation (Putnam 1993). Examples of cooperative norms range from the relatively simple, such as littering to prime features of a functional society, such as the enforcement of property rights. These norms also reduce the costs of monitoring and enforcement of social or economic malpractice.

**Table 3.3: Perception of company ethics and Return on Asset (RoA) modelling results**

Dependent variable:	Return on Assets
Governance	0.010* (0.006)
Lagged Return on Asset	0.067 (0.046)
Constant	-0.014 (0.34)
Year fixed effects	Yes
Industry controls	Yes
Company fixed effects	Yes
No. of observations	338
R <sup>2</sup>	0.458

Source: Deloitte Access Economics (2020) modelling. Note: \*, \*\*, \*\*\* mean statistically significant at the 10%, 5% and 1% level respectively. Results for company, industry and time fixed effects are not presented here for brevity.

**Chart 3.2: Cross-country correlation between trust and GDP per capita (ln)**



Source: World Values Survey (2010-2016), European Values Survey

Empirical papers, starting with Knack & Keefer’s (1997) seminal work,<sup>51</sup> have confirmed that trust does appear to constitute a decisive determinant of growth. Importantly, these authors point out that this is not a one way effect. It is accepted that economic growth and development may also influence trust in a society.

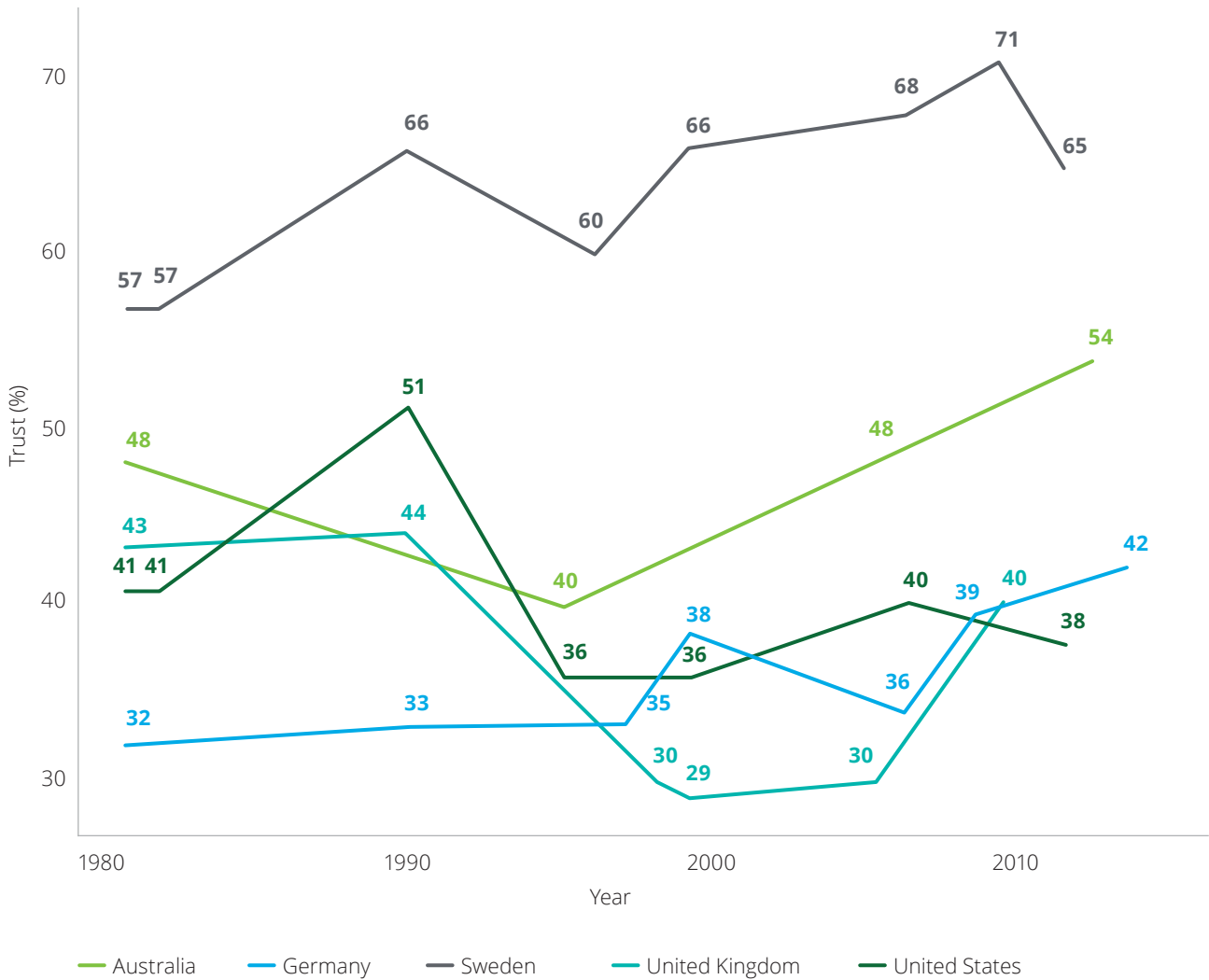
Chart 3.2 plots the average GDP per capita (log) against the average trust for a sample of 59 countries between 2010 and 2016. Countries with higher levels of trust also tended to have higher income levels. Approximately one-fifth of the cross-country variation in GDP per capita is related to the differences in trust levels.

While there is a strong correlation between the level of trust and economic performance across countries, there are two points to discuss before proceeding with econometric modelling. The first is reverse causality. Trust is likely to be influenced by the economic development of a country. For example, citizens of a country with a well-performing economy may be more likely to trust their fellow citizen because things are going well.

To help address this potential reverse causality, the model in this report uses ‘historical trust’ as the variable of interest. The use of historical trust draws from the theory of the transmission of values.<sup>52</sup> Current values are shaped by the current environment as well as beliefs inherited from earlier generations. Our model uses the time variation inherent in historical trust to estimate trust’s effect on economic performance.

The second point to discuss is how other variables might codetermine both trust and economic performance. In particular, institutions and geography have been found to affect economic performance.<sup>53</sup> These factors are controlled for by their inclusion in our model as well as the inclusion of country and time fixed effects.

Chart 3.3 Timeseries of selected countries trust levels, 1980-2016



Source: World Values Survey (2010-2016), European Values Survey

**3.2.3.2 Trust in Australia**

Australia has tended to have higher levels of trust compared to peer nations such as the USA, the UK and most Western European countries. However, Australia has consistently fallen behind the Scandinavian countries of Sweden, Norway and Finland as shown in Chart 3.3.

Since 1995, when only 40 per cent of Australians said they trust other people, average levels of trust have grown steadily. In 2012<sup>54</sup> 54 per cent of Australians noted that they generally trust other people that they interact with. This was a considerably higher percentage than the USA, the UK and Western European nations but was approximately 10 percentage points lower than Sweden, the country with consistently one of the highest levels of trust.

The results of our modelling indicated that if Australia were to increase its level of trust to Sweden's level, or approximately 10% then average annual incomes would increase by approximately \$1,800. **This equates to a net increase in total incomes across Australia of approximately \$45 billion (2020 dollars).**<sup>55</sup> These annual benefits would grow towards these levels as the country moved towards higher levels of trust.

This result is the more conservative estimate from models including lagged trust as a measure of trust and after controlling for population, the price of investment goods, the economic freedom index, the polity V index and lagged human capital.

An alternative model was estimated using current levels of trust and country fixed effects and resulted in an estimated increase in average annual income of \$700

per person if Australia's ethical level rose to that of Sweden. Results from all of these models are set out in Appendix C.

Given that changes in trust amongst a population tend to shift slowly over time (an exception may apply in instances of large external shocks, such as natural disasters or severe economic downturns) one would expect that the economic benefits presented above would similarly take effect over the long-term.

The finding that higher levels of trust are also associated with higher GDP per capita may imply that some countries have a degree of trust premium such that others may be more likely to trade with them if they are perceived to be more trustworthy. To the extent that there is such a premium, it may decline if trust improves across a range of countries.









## 4. Improving ethics in Australia

The preceding chapters of this report have demonstrated the value of ethics to our economy and society. This chapter sets out a range of recommendations to help improve ethics in Australia drawing on research and consultation with leaders in government, business and civil society.

Ultimately, improving ethics requires a multifaceted and coordinated approach. The complexity of ethical decision-making, and the infrastructure needed to support it, means improving ethics cannot be achieved with a single initiative.

And even as our ethical infrastructure is designed and strengthened, an element of fragility will always exist. Not all behaviour can be codified, and there is always a risk that individual actions will undermine confidence in the supporting ethical infrastructure, either in part or as a whole.

Recognising these inherent challenges, there are a number of potential initiatives which can help improve ethics in Australia. The level of ethics is not simply an unalterable endowment in society; just as it can be eroded overtime, so too can it be improved.

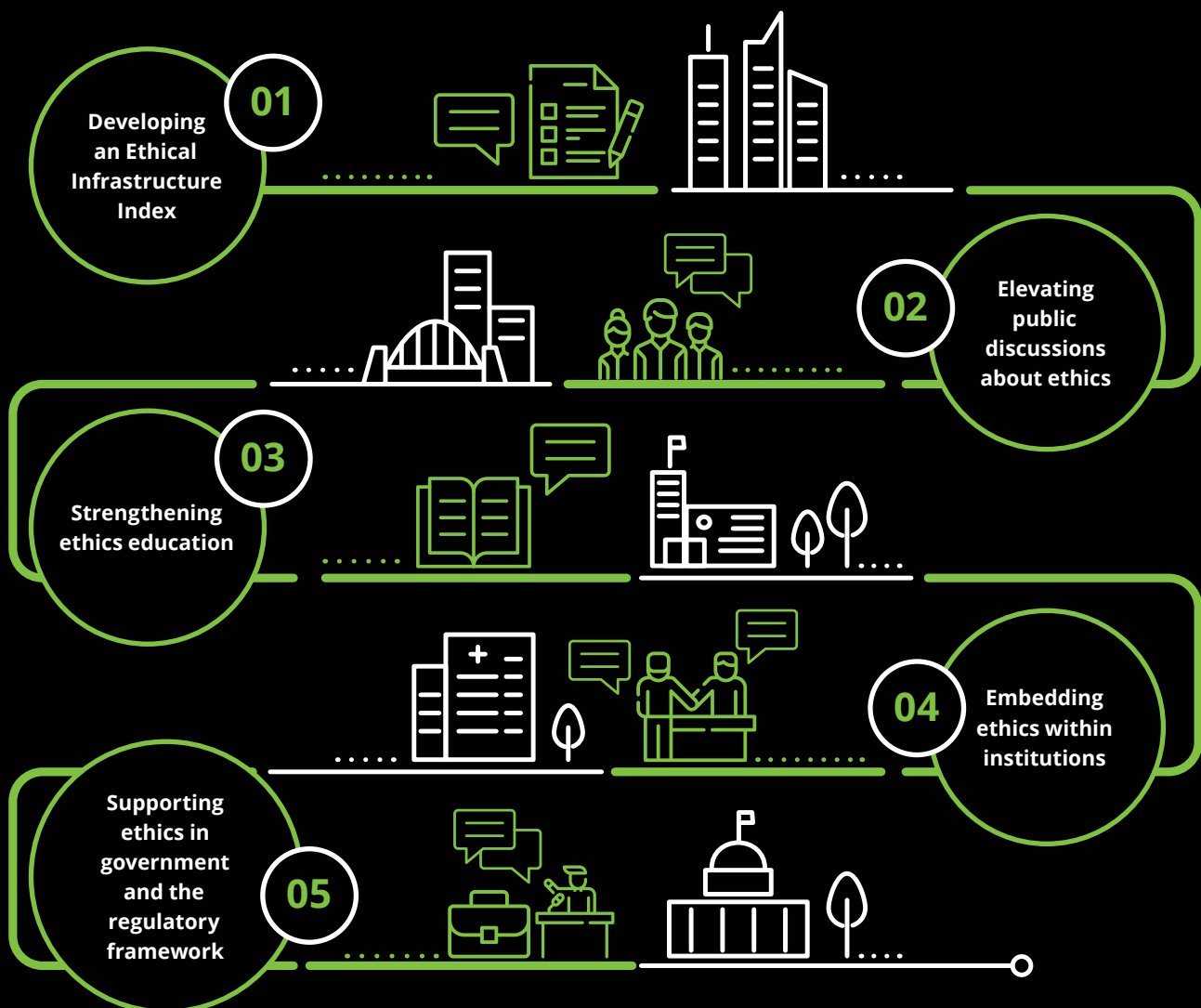
It is important to recognise that these recommendations are intertwined. The final section of this Chapter discusses how these recommendations can help Australia in addressing some of its most pressing current and future ethical challenges.

### 4.1 Developing an Ethical Infrastructure Index

While there is some acknowledgment about the importance of ethics to different sectors and to society more generally, Australia would benefit from more explicit endorsement by leaders. This could take the form of a National Ethics Framework (of core values and principles) against which we could measure the alignment of our national ethical infrastructure – in whole and in part. Such an aspiration would raise the profile of ethics and allow it to be monitored more effectively. We note here that the development of a national Framework may offer an important further opportunity to draw on the insights of Australia's First Nation's peoples – who would offer a perspective uniquely attuned to this Continent.

The development of a National Ethics Framework could also help to drive a distinctly Australian ethos – and offer a touch point for calibrating efforts to preserve national coherence without sacrificing the strengths derived from a multicultural society. It may also help with foreign policy. Strengthening a broad set of alliances within and across our region will require Australian diplomacy to be less 'transactional' and more relational. In turn this will be aided by Australians having a clear sense of who we are and what we stand for in our region and by investing in telling Australian stories. Finally, our actions (both at home and abroad) will need to be seen to accord with our declared values and principles – otherwise we will never fully enjoy the trust and confidence of other countries on whom we rely.

# Our recommendations fall into the following five categories:





“People make ethical decisions every day. We do good things and avoid bad things. But most don’t have the language to understand this as ethics.”

**Hugh Breakey**

It is important that there be broad community consultation in setting this Framework. A government pronouncement on ethics could be viewed cynically by a public that already has considerable distrust of politicians. This national framework should sufficiently accommodate the diversity of views and beliefs held in the community and not seek to set an overly prescriptive standard.

Specific measures:

- Australia should set a core Australian Ethics Framework. This should be supported by clear progress metrics, such as improving the decision making capacities of leaders, embedding ethics within institutions, and improving ethics education.
- Organisations throughout business and civil society should publicly endorse this Framework and outline initiatives to improve ethics within their organisation.

#### **4.2 Elevating public discussions about ethics**

Similarly, leaders in government, business and civil society commented that the language of ethics is not understood or discussed regularly in everyday situations. Whenever people make decisions about things that are good, bad, right or wrong, they use (perhaps unknowingly) the language of ethics. But the ability to reflect on, articulate and discuss the ethically important features of situations is limited. This is supported by research showing that, in general, people are not good at justifying their ethical commitments.<sup>56</sup>

Research on the contextual influences of ethical behaviour suggests that people are more likely to act ethically when they are reminded of their ethical principles.<sup>57</sup> If debates about ethical issues were more common in public spaces, such as in the media, people would likely be more attuned to seeing ethics within their own lives and be able to discuss issues in their everyday contexts.

Specific measures to elevate public discussions about ethics in Australia:

- More public or industry specific forums to discuss ethical issues. The Ethics Alliance and the Global Compact Network Australia are current examples of business forums providing space for leaders to reflect on past experiences, share good and bad practices and learn from their peers.
- Creation of an annual ethics survey or ranking to be published by a media organisation. This may be similar to the AFR’s annual ‘Power List’ of Australia’s most influential people, or the annual ranking of top graduate employers. This list could be based on surveys about community perceptions of ethics, and what influences these perceptions. While providing one metric of ethics will be difficult, such a list would make conversations about ethics and its importance more commonplace. It may also allow organisations to better appreciate the economic benefit that can come from ethics, and initiatives to improve their ranking.
- Measures to maintain the quality of journalism. This could include improving ethics training for journalists in university as well as considering funding options to provide greater scope for more extensive investigations by the media to encourage fair and accurate reporting. Key to driving more public debates on ethical issues is for the media industry and journalists to better understand the ethical tensions inherent in their work and how to use the language of ethics to facilitate a more effective discussion of issues.

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“Australia is less overtly religious than other countries, but ethical values are still strong. There needs to be more open conversations and public debate about ethical issues. This will help people realise it’s not just about religion or moral relativity, and be able to apply this thinking to their own lives.”

**Professor Ian Harper, Dean of Melbourne Business School**

### 4.3 Strengthening ethics education

Ethics is a skill that can be developed through education and training, across primary, secondary and tertiary institutions, and by promoting ethics within professions.

#### 4.3.1 Ethics education in schools and universities

Ethical Understanding is one of seven General Capabilities identified in the Australian Curriculum for all primary and secondary schools in Australia.<sup>58</sup> It involves the ability to “identify and investigate the nature of ethical concepts, values and character traits, and understand how reasoning can assist ethical judgement.”<sup>59</sup> Ethics and philosophy classes are not common in primary and high schools in Australia.<sup>60</sup> Increasing the number of ethics and philosophy classes in primary and high school curriculum or the integration of ethics into the mainstream curriculum will contribute to specific educational capabilities such as thinking skills, creativity and ethical behaviour.<sup>61</sup>

In Australian universities, ethics courses are mostly taught as standalone modules within philosophy majors, as well as being integrated within several professional disciplines like legal practice, medicine, nursing and engineering. While there are some benefits to understanding abstract theory, ethical conduct is most likely to result when teaching is case study based and contextual. Damon (1997) presents research indicating that ethics courses are most effective when integrated into other coursework, and are supported by faculty. This helps develop an ethical culture in students, promoting ethics as something lived and practical, rather than an add on or box ticking exercise.

Specific measures:

- In primary schools, expanding Primary Ethics to all states and territories in Australia, and including it as a standalone subject as is done in countries like The Netherlands.<sup>62</sup>
- In secondary schools, including philosophy as a subject or otherwise integrating ethics into the curriculum throughout high school and for all leaving-school certificates.<sup>63</sup>
- In universities, focussing on ethics courses that are integrated into other coursework, rather than as standalone units.<sup>64</sup> Ethics could be a foundational subject integrated into all degrees.
- Increasing the number of philosophy and ethics educators across all levels of education, with a focus on teaching ethics in a way that is practical and engaging.

#### 4.3.2 Ethics education in the workplace

Ethics education is important for professionals and government, business leaders and civil society. Understood as a skill, professional ethics goes beyond compliance and describes the capacity to deal with ambiguous or risky situations in a way that is principled and is aligned with the organisation’s values.

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“It is impossible to codify every situation, so laws and compliance can only go so far. We don’t need more codes of ethics, instead we need to develop the capacity for people to understand their internal bargaining system and hidden psychological drivers when making decisions.”

**Megan Motto, CEO of Governance Institute**

While an institution’s formal systems, processes and procedures should be designed in ways that encourage (and at least do not undermine) ethical behaviour, the capacity of individuals within institutions is also vital and can be developed. Improving the capacity of individuals and leaders goes hand in hand with improving formal systems, as outlined below. Professional ethics can be improved through case studies and industry specific examples, and it is crucial to developing and maintaining trust between staff members, with customers and with suppliers.

#### **4.4 Embedding ethics within institutions**

While all the initiatives outlined in the recommendations for this report will improve Australia’s ethical infrastructure, embedding ethics within institutions is particularly important. As chapter 2 describes, designing strong ethical infrastructure involves shaping systems and the environment to encourage ethical behaviour and inhibit unethical behaviour. It involves both formal and informal elements, and being conscious of the way in which context shapes choice. This acknowledges the ethical fallibility of people’s natures, and how power imbalances can create unethical situations such as between customers and firms, management and shareholders.

#### **4.4.1 Governance and systems**

Part of ethical infrastructure is about designing institutional systems that encourage ethical performance and decision making and discourage poor behaviour. These systems, procedures and policies may include things like statements of purpose, values and principles (the principal components of an ethics framework); related codes of conduct, HR systems (onboarding and offboarding procedures, remuneration, incentive structures, consequent management structures); risk and audit structures (risk management frameworks, audit processes); IT systems (including AI Ethics); and any other systems or structures that activate and support decision making within a business.<sup>65</sup> As noted in our case study on the finance sector, many of the issues uncovered in the 2019 Banking Royal Commission were driven by perverse incentive structures – highlighting the importance of reforming systems to enhance ethical behaviour.

If done effectively, these systems create the conditions in which people are supported to make ethical choices. Trevino and Nelson (2011) outline that an ethical culture includes formal and informal systems aligned to support ethical judgement and action.<sup>66</sup> This creates the psychological safety needed for people to feel able to speak up freely, both lowering the risk of unethical conduct going unnoticed, and increasing collaboration.<sup>67</sup> It is where people do things for the right reasons, lowering compliance and transaction costs and encouraging innovation.







# How to best teach ethics?

A consistent theme throughout consultations was that some methods of teaching and promoting ethics are more effective than others. This is true both in professional settings, and in universities and schools.

Hugh Breakey, President of the Australian Association for Professional and Applied Ethics and Senior Research Fellow at Griffith University, spoke about the most effective ways of teaching ethics.

Similar to consultees across industry, Breakey said that in workplaces and professional settings, case studies and specific examples about ethical issues are far more impactful than prescriptive rule books. Abstract philosophical theory or general ethics frameworks can be helpful in certain situations to dissect ethical dilemmas, but in general, contextual training and discussing issues with others is more likely to lead to the deliberation and ethical reasoning skills that leads to ethical conduct.

Another common theme in research is the importance of utilising and enhancing the ethical capabilities that we all already have within us. Teaching ethics should be 'bottom-up', where individuals are encouraged to reflect on their own values and experience and bring this to their decision making, rather than a 'top-down' where rules or principles are proscribed.

"Our ethical outlook is deeply shaped by our personal values and what we have grown up with. Acting in line with our values and commitments is a good thing, which means that for robust ethical decision making you need to consult widely and have a diversity of perspectives."

**Nev Power, Head of the COVID19 Coordination Commission**

"There is a rich and diverse set of values within Australia's multicultural society. People should be encouraged to bring these experiences and values (be they religious, cultural, gender-based etc.) into the decision making process. This cultivates a richer experience of collective decision making, creates more engagement with ethics, and it's also good for encouraging pluralism within our democracy."

**Dr. John A. Rees, Professor of Politics & International Relations at the University of Notre Dame Australia**





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“Codes of conduct are getting longer and longer every year. People are not moral vacuums – they have strong values informed by their parents, upbringing, community. Organisations should draw on these strengths rather than creating more elaborate rulebooks.”

**Glenn Stevens, former RBA Governor**

“In the public sector, there are more than enough codes of conduct and ethics handbooks. What is needed is practical training, instruction and debate, both within the community and government.”

**Michael Barnes NSW Ombudsman**

It is important that ethics within organisations is not confused with compliance, which it often is. Compliance is narrower, and generally focuses on telling people what not to do, rather than empowering people to think critically, decide and act. In fact, compliance regimes can encourage a tick-the-box mentality, and often have the effect (intentionally or otherwise) of enforcing conformity and discouraging people from thinking critically. However, compliance can play a role in ensuring minimum ethical standards are upheld.

Specific measures:

- Review codes of conduct to make sure they are up to date, have buy-in from business/organisational leadership, use plain English and case studies to communicate and are of a length that shows they are serious (more than 5 pages) but not excessively long. And make sure they cover key issues (with reference to, for example, the ASX's 8 principles for corporate governance).
- Create or improve business/organisational whistleblower policies so that they are accessible 24/7, including to contractors/suppliers, can offer anonymity and protections against retaliation.
- A broader review of structural measures that shape behaviour, including: economic incentives, organisational values, principles and goals, compliance and punishment and reward systems and HR policies. Aligning these measures in the direction of good ethical behaviour.
- Greater focus on developing positive ethical cultures within organisations, including establishing an aspirational culture, ensuring board and executive buy-in, measuring current state and executing change activities to move towards the aspirational culture.

# Principles for corporate governance

The ASX Corporate Governance Principles and Recommendations 4th Edition February 2019<sup>68</sup> sets out eight principles for corporate governance:

1. Lay solid foundations for management and oversight: A listed entity should clearly delineate the respective roles and responsibilities of its board and management and regularly review their performance.
2. Structure the board to be effective and add value: The board of a listed entity should be of an appropriate size and collectively have the skills, commitment and knowledge of the entity and the industry in which it operates, to enable it to discharge its duties effectively and to add value.
3. Instil a culture of acting lawfully, ethically and responsibly: A listed entity should instil and continually reinforce a culture across the organisation of acting lawfully, ethically and responsibly.
4. Safeguard the integrity of corporate reports: A listed entity should have appropriate processes to verify the integrity of its corporate reports.
5. Make timely and balanced disclosure: A listed entity should make timely and balanced disclosure of all matters concerning it that a reasonable person would expect to have a material effect on the price or value of its securities.
6. Respect the rights of security holders: A listed entity should provide its security holders with appropriate information and facilities to allow them to exercise their rights as security holders effectively.
7. Recognise and manage risk: A listed entity should establish a sound risk management framework and periodically review the effectiveness of that framework.
8. Remunerate fairly and responsibly: A listed entity should pay director remuneration sufficient to attract and retain high quality directors and design its executive remuneration to attract, retain and motivate high quality senior executives and to align their interests with the creation of value for security holders and with the entity's values and risk appetite.





“To have an ethical organisation, you need to have ultra-ethical leaders.”

**Grant Hehir, Auditor General**

“Leaders set the tone and create trust within organisations.  
The moment you can’t trust, you can’t respect, you can’t serve.”

**Andrew Scipione, former commissioner of NSW Police Force**

#### 4.4.2 The critical role of leaders

Leaders shape an organisation’s culture and serve as role models for good behaviour. Even organisations with the strongest systems, policies and procedures will struggle to maintain ethical conduct if poor behaviour is modelled by leadership. People are shaped by those around them and those in positions of power have particular influence. Indeed, in some settings (such as the Australian Defence Force) leadership is defined as, itself, an ethical practice.

Leaders should be viewed as ethical champions whose role it is to ensure that the purpose of an organisation is understood and amplified by those who work for them. Leaders themselves need to be ethical, understanding their obligations to their organisation and not acting in self-interest. Tone at the top needs to cascade down into business. And leaders need to have the self-awareness to reflect on decisions and be open and willing to accept mistakes, and create psychological safety for their people to do the same.

Specific measures:

- Embedding ethical performance metrics within HR systems and promotions.
- Improving the capacity of leaders to speak openly about ethical issues. This includes setting an ethical vision for their organisation or team, and developing the ability to reflect on past decisions.
- Leaders communicating the rationale of decisions to affected stakeholders.
- Leaders communicating on lessons learnt and creating an environment of psychological safety to enable others to speak up about ethical issues they have identified.
- Ethics training for leaders. Teaching skills such as embedding conversations about ethics and culture within everyday work contexts and linking this to supporting the organisation’s purpose and values. Teaching collaboration skills, and the importance of stakeholder inclusiveness in making decisions – stronger diversity of perspectives means more robust and ethical decision making

#### 4.4.3 The benefits of purpose

A strong sense of occupational or industry purpose has many benefits including greater employee engagement and improved organisational culture. Leaders play an important role in cultivating purpose within their teams and modelling an organisation's values. They can do this by bringing discussions about purpose into projects and team meetings, and encouraging employees to reflect on their own values and aspirations.

Industries or organisations with a clear sense of purpose are likely to exhibit stronger ethical norms. While professionalisation instils these norms formally through a governing body and agreed industry standards, cultivating a clear moral compass and sense of purpose is an informal and effective way of maintaining ethics. We note that the role of business in society is contested ground - with Milton Friedman famously arguing that the social responsibility of business is to increase profits (albeit within the rules of the game).

Specific measures:

- Leaders and organisations should encourage employees to think about how they gain meaning from their work, what their individual purpose is and how this fits within organisation's purpose, values, principles and goals. This improves employee engagement, and helps to develop an ethical culture where norms are upheld and the purpose and values of an organisation are lived.

#### 4.4.4 Professionalisation

The professionalisation of occupations can play a role in introducing ethical standards and promoting ethical decision-making. This is one step further than professional ethics as a skill, and can be seen as a formal way of instilling 'purpose'.

Professionalising an occupational group has many benefits, including the work done by an oversight body and clearer articulation and awareness of industry ethical norms and standards. Professionals hold each other to account and where standards are violated, consequences can include expulsion. While there are common underlying ethical themes in different contexts (like being honest, respectful and fair), some occupations have their own codes. For instance, codes for lawyers focus on fairness and the proper administration of justice, whereas for healthcare workers it is about duty of care to patients, avoiding harm and promoting well-being. Professionalisation of certain industries and occupational groups has significantly raised ethical standards. Medicine and law are historical examples. More recently, police, and the push for professionalisation of financial advice industry, post GFC, provide further examples.

In making this recommendation it is important to note that professionalisation can have both costs (in the form of increasing barriers to entry) as well as benefits in improving ethics standards. Any move to professionalisation should be undertaken in ways that maximise the benefits of professionalisation while minimising potential costs.

Specific measures:

- Expanding industry specific and case-study based ethics education across all industries to improve the 'professional ethics' capacity of the workforce.
- Increased professionalisation of industries to solidify ethical norms and governance, such as for financial advisors.

#### 4.5 Supporting ethics in government and the regulatory framework

Government obviously has a huge role to play in encouraging ethical behaviour; it is an ethical benchmark, a regulator, and has an array of institutions including departments, agencies, and corporatize entities.

When most people think of 'the government' they are thinking about politicians that make up the executives in federal and state governments. Initiatives to reduce unethical behaviour by political leaders and political parties would help restore trust in Australia's democracy. Many of the available tools are well-known, including: reforms to political donations, lobbying activity, appointment processes, electoral laws, codes of conduct and integrity bodies.

Improving policy-decision-making processes would also lift ethics in government. This involves a process that is evidence-based, includes appropriate consultation, is guided by a framework that fairly considers all stakeholders, and that is transparent, subject to debate and, where appropriate, review. One example of improvement here was fiscal transparency achieved by the Charter of Budget Honesty. Another important area is Freedom of Information (FoI) laws. Ethical policy making and funding decisions should ideally occur without undue influence from lobby groups or political forces (e.g. 'pork-barrelling').

For example, Michael Barnes, the NSW Ombudsman, recommended that the government develop systems to guide decision-making which set out the range of stakeholders and factors that need to be taken into account in any decision made by a public servant. Such systems would ensure that decisions take into account potential impacts and consequences for a range of actors and could be used to limit the scope for lobby groups to argue that particular factors were not taken into account in decision-making.





The introduction of a Federal Integrity Commission is another initiative which has widespread political support. The Federal Government released a consultation paper earlier this year although the process was put on hold as a result of COVID-19. As the government restarts this process it will be important to consider the scope of the Commission's powers. The five Beechworth principles state that such a Commission must have: broad jurisdiction; common rules; appropriate powers; fair hearings and public accountability provide a sound basis for considering the development of a Federal Integrity Commission and ensuring it is well placed to enhance ethics in government.

Government regulations can also help businesses and other organisations to act ethically. While entities should be encouraged to act ethically on their own accord, sometimes regulation is needed. In particular, market pressures can provide powerful disincentives to act ethically if a firm believes its competitors will simply continue with 'business as usual'. In such situations, industry-wide regulation makes it easier for all firms to do what is right. Market pressures on ethics can be especially strong in highly concentrated markets, which create more opportunities for powerful firms to act against the interests of consumers, suppliers or the public (some of which conduct might be unethical). Strong whistleblower protection can help uncover unethical behaviour within organisations, and regulation to support safe disclosures can help firms do the right thing.

Government agencies could also incentivise more ethical structures within businesses through their procurement processes. Governments could apply a form of 'ethical conditionality' around the provision of government funding on the basis that better ethics will provide a better return for the taxpayers' investment. Some applications for government support could include a section outlining the applicant's approach to ethics. Such measures could be strengthened, such as by requiring independent assurance to determine the extent to which ethical processes are followed in practice.

Specific measures:

- Reconsider Australia's system for regulating political activity including electoral laws, political donations, lobbying, integrity bodies and Ministerial codes of conduct.
- Strengthen policy decision-making processes to ensure they are evidence-based, transparent, consider stakeholders, involve consultation, and are made without undue influences.
- Ensuring the independence and effectiveness of industry regulators. Maintaining appropriate funding for regulators so they can limit industry concentration, prevent conflicts of interest and drive accountability.
- Establishing a Federal Integrity Commission that has appropriate powers and a broad jurisdiction.
- Strengthening whistleblower legislation and awareness of legislation in the public. Championing the courage of whistleblowers to incentivise people speaking up.
- Improving transparency about the reasons for decision making, especially in areas where governments have high levels of confidentiality such as national security and health. One part of this is FoI laws - stronger FoI laws would provide benefits such as increased transparency.
- Promoting ethical cultures and ethical decision making in government by focussing on culture measurement and leadership development.
- Using the purchasing power of government to encourage and reward ethical conduct by entities in its supply chain and those seeking government funding more generally.
- Strengthening measures for the government to manage conflicts of interest and probity rules.

#### 4.6 Applying ethics to Australia's future challenges

Through consultation with leaders in government, business and civil society, three key ethical issues for Australia's future were identified – reconciliation with Australia's First Nations people, climate change and the environment, and technology and artificial intelligence.

This section discusses how this report and the recommendations in this chapter can be used to help address these issues. In particular, establishing a national Ethics Framework, elevating public discussions about ethics, and promoting ethical leadership will play an important role in increasing awareness of these issues, and consequently develop Australia's capacity to embrace and make the most of change.



#### 4.6.1 Reconciliation with Australia's First Nations people

Indigenous Australians are the most incarcerated peoples in the world. Colonisation and dispossession since the Eighteenth Century have led to ongoing health, economic and social disadvantage.

As the Uluru statement from the heart urges, a process of truth telling is required for Australia to heal its wounds of the past. "We must hear and know the truth of the past before we can address it." Committing to truth telling about the nation's history and the change needed allows for people to walk forward together.

- Elevating public discussions about ethics and improving Australia's ethical literacy will help non-Indigenous Australian's to appreciate their obligations to Australia's Traditional Owners and their role in reconciliation.
- Improved ethical leadership will likely lead to greater stakeholder collaboration and listening to Indigenous Australian voices regarding public policy.
- Indigenous Australian perspectives can and should inform the development of a distinctly Australian national Ethics Framework.

#### 4.6.2 Climate change and the environment

Addressing climate changes is one of the biggest challenges facing humanity. In Australia, the economic cost of climate change and extreme weather in the form of loss of property value has been estimated to accumulate to \$571 billion by 2030.<sup>69</sup> This is in addition to the the cumulative loss of wealth from the impacts of climate change on agricultural and labour productivity, which has been estimated to reach \$4.2 trillion by 2100 in Australia.<sup>70</sup> Australia has already experienced increases in average temperatures over the past 60 years, with more frequent hot weather, fewer cold days, shifting rainfall patterns and rising sea levels. Collective effort from various stakeholders in society is required to address such a significant challenge.

- Elevating public discussions about ethics and strengthening ethics education will allow people to better appreciate the risks of climate change to future generations and mould behaviour and decisions to address climate change accordingly.

#### 4.6.3 Technology and Artificial Intelligence

As technologies such as Artificial Intelligence (AI), robotics and gene editing continue to have a growing impact on all aspects of society, there is a need to understand the ethical design and deployment of these powerful drivers of change. This will ensure important social values like trust are maintained, as well as protecting individual rights like the right to privacy and the right to be forgotten. Failure to get the ethics right will erode trust. In turn this is likely to increase the risk that society will reject technologies that would otherwise improve the lives of all.

- Embedding ethics within institutions will encourage ethics to be considered defacto in the design, development and deployment of new technologies. Increasing transparency about the design of technologies (not least in the collection and use of data) will increase trust, which strengthens the social license for new technologies.
- Elevating public discussions about ethics and strengthening ethics education will allow the public to better evaluate the ethics of new technologies and demand certain principles are met.

# Appendix A: Modelling the individual benefits of ethical behaviour

This section outlines the econometric techniques used to examine the association between measures of ethical behaviour and labour market and health outcomes at the individual level.

As noted in 3.2.2 above, the analysis was performed using data from the HILDA survey. To obtain a measure of ethical behaviour, we constructed an individual and a region-based ethical behaviour perception index, using individual responses to the three following statements about perceptions of ethical behaviour in the survey:

- Most people you meet keep their word;
- Most people you meet make agreements honestly; and
- Most people you meet succeed by stepping on other people.

The responses, which were scores between 1 (“Strongly disagree”) to 7 (“Strongly agree”) indicating levels of agreement with the statement, were recoded (so that higher scores correlated with a stronger perception that there was positive ethical behaviour), rescaled between 0 and 6 and then aggregated. This produced an individual-based ethical behaviour perception index measured between 0 and 18. We then grouped individual ethical behaviour scores by region and by year, and generated mean regional ethical behaviour scores. These mean scores were then assigned to each individual, depending on which region they were living in in a given year, to create a regional ethical behaviour index. Responses to these variables were captured in waves 6, 8, 10, 11 and 14.

As a further robustness check, Deloitte Access Economics also considered an additional measure of ethical behaviour, using individual responses to the following statement in the HILDA survey:

- Most people would try to take advantage of you if they got a chance.

Responses to this statement also ranged scores between 1 (“Strongly disagree”) to 7 (“Strongly agree”) indicating levels of agreement with the statement. As higher scores indicated a stronger perception that there was negative ethical behaviour, all responses were reverse coded and then rescaled to a scale of 0 to 6 to produce an individual-based measure of perceived ethical behaviour. Mean regional scores by year were then generated and assigned to individuals based on their regional location in a given year to create a region-based measure of perceived ethical behaviour. An advantage of this variable is that it is captured in an additional wave (wave 5).

The key labour market outcomes we considered were an individual’s likelihood of employment and their wage level, which are also collected by the HILDA survey. The key health outcomes we considered were an individual’s general health, physical health and mental health scores, also taken from the HILDA survey. These were all measured between 0 and 100, with higher scores indicating better perceived health.



## A.1. Methodology

### A.1.1. Individual health outcomes

To estimate the relationship between ethical behaviour and individual health outcomes, the following specification was used:

$$y_{it} = \alpha + \beta EB_{it} + \gamma X_{it} + u_i + \varepsilon_{it} \quad (1)$$

where  $y_{it}$  indicates an individual  $i$ 's general, physical or mental health outcome at time  $t$ ,  $EB_{it}$  is their individual perception of ethical behaviour in the people around them at time  $t$ ,  $X_{it}$  is a vector of individual demographic characteristics,  $u_i$  is an individual fixed effect (the unobserved difference in an individual's health or employment outcomes) and  $\varepsilon_{it}$  is a random error term.

Equation (1) was estimated using regression analysis. As all health measures – general, physical and mental – were continuous, regressions were estimated using a linear regression model with individual fixed effects.

In general, a model with fixed effects is likely to be preferable as they control for potential unobservable characteristics which may make individuals inherently more (or less) likely to be in good health. In other words, individual fixed effects help control for the possibility that individuals with strong positive perceptions of ethical behaviour may also have other innate characteristics which lead them to have intrinsically better health outcomes. By including individual fixed effects, the identifying variation is coming from changes in a given individual's ethical behaviour index on individual health outcomes.

### A.1.2. Individual labour market outcomes

To estimate the relationship between ethical behaviour and individual labour market outcomes, the following specification was used:

$$y_{it} = \alpha + \beta REB_{it} + \gamma X_{it} + u_i + \varepsilon_{it} \quad (1)$$

where  $y_{it}$  indicates an individual  $i$ 's employment or wage outcome at time  $t$ ,  $REB_{it}$  is the regional ethical behaviour index score for the region the individual is located in at time  $t$ ,  $X_{it}$  is a vector of individual demographic characteristics,  $u_i$  is an individual fixed effect (the unobserved difference in an individual's employment or wage outcomes) and  $\varepsilon_{it}$  is a random error term.

Like equation (1), equation (2) was estimated using regression analysis. The modelling specifications adopted differed depending on form of the dependent variable being considered. In the case of employment, where the form of the dependent variables take a value of 0 or 1, models were estimated using a logit model both with random effects and subsequently controlling for individual fixed effects. In the case of the wages, which are non-binary, regressions were estimated using a log-linear regression model with both random effects and subsequently controlling for individual fixed effects.

Again, a model with fixed effects is likely to be preferable as they control for potential unobservable characteristics which may make individuals inherently more (or less) likely to be employed or have a higher income, and also be correlated to the individual's choice of location in a region with certain levels of ethical behaviour. In other words, individual fixed effects help control for the possibility that individuals located in regions with higher levels of perceived ethical behaviour may also have other innate characteristics which lead them to have better labour market outcomes.

However, it is worth noting that as ethical behaviour is only recorded in a small number of waves there are relatively few observations per individual- and often individual's employment status does not change across waves. Moreover, while there is some variation over time in regional measures of ethical behaviour this variation usually occurs within a relatively small band. Thus in including individual fixed effects there may be limited identifying variation within individuals to examine the relationship between ethical behaviour and employment status.

## A.2. Results

### A.2.1. Ethical behaviour and individual health outcomes

Table A.1 reports the estimated regression results where the dependent variable is self-reported general health. These results imply that a one unit increase in an individual’s perception of ethical behaviour is associated with a 0.4 to 0.5 unit improvement in self-reported general health scores.

**Table A.1: Estimated regression results for self-reported general health**

<b>Dependent Variable:</b>	<b>General health</b>	
<b>Model specification:</b>	<b>OLS model with FE</b>	<b>OLS model with FE</b>
Age	-0.541*** (0.019)	-0.490*** (0.017)
Education		
• Post-graduate qualification	0.540 ζ(0.8987)	1.022 (0.903)
• Graduate diploma	0.582 (0.923)	1.600** (0.838)
• Bachelor or Honours degree	0.831 (0.608)	0.937** (0.554)
• Advanced diploma	0.899 (0.731)	1.229** (0.690)
• Certificate III or IV	0.534 (0.459)	0.567 (0.433)
• Completed year 12	1.099*** (0.359)	-0.995*** (0.338)
Employed	1.187*** (0.192)	1.195*** (0.184)
Married	0.327 (0.243)	0.207 (0.229)
Has children aged 0 to 14 years	-0.139 (0.249)	0.003 (0.179)
<b>Individual ethical behaviour index</b>	<b>0.417*** (0.023)</b>	
<b>Individual perception of advantageous behaviour</b>		<b>0.548*** (0.041)</b>
No. of observations (n)	64,006	64,725

Source: Deloitte Access Economics modelling.

Note: \*\*\*, \*\*, \* indicate statistical significance at the 1%, 5% and 10% level, respectively.

Table A.2 reports the estimated regression results where the dependent variable is self-reported physical health. These results imply that a one unit increase in an individual’s perception of ethical behaviour is associated with a 0.1 unit improvement in self-reported physical health scores.

**Table A.2: Estimated regression results for self-reported physical health**

Dependent Variable:	Physical health	
Model specification:	OLS model with FE	OLS model with FE
Age	-0.543*** (0.024)	-0.488*** (0.021)
Education		
• Post-graduate qualification	4.736*** (1.193)	4.427*** (1.074)
• Graduate diploma	4.033*** (1.117)	3.592*** (0.992)
• Bachelor or Honours degree	3.669*** (0.736)	3.242*** (0.657)
• Advanced diploma	4.354*** (0.886)	3.877** (0.818)
• Certificate III or IV	3.593*** (0.555)	3.087*** (0.512)
• Completed year 12	2.740*** (0.435)	2.327*** (0.400)
Employed	2.112*** (0.232)	2.095*** (0.217)
Married	0.743** (0.293)	0.940*** (0.270)
Has children aged 0 to 14 years	0.617*** (0.229)	0.701*** (0.211)
Individual ethical behaviour index	<b>0.140*** (0.028)</b>	
Individual perception of advantageous behaviour		<b>0.114** (0.048)</b>
No. of observations (n)	64,426	66,585

Source: Deloitte Access Economics modelling.

Note: \*\*\*, \*\*, \* indicate statistical significance at the 1%, 5% and 10% level, respectively.

Table A.3 reports the estimated regression results where the dependent variable is self-reported mental health. These results imply that a one unit increase in an individual’s perception of ethical behaviour is associated with a 0.6 to 0.8 unit improvement in self-reported mental health scores.

**Table A.3: Estimated regression results for self-reported mental health**

<b>Dependent Variable:</b>	<b>Mental health</b>	
<b>Model specification:</b>	<b>OLS model with FE</b>	<b>OLS model with FE</b>
Age	-0.081*** (0.019)	-0.070*** (0.017)
Education		
• Post-graduate qualification	-1.462 (0.970)	-0.104 (0.878)
• Graduate diploma	-0.905 (0.907)	0.279 (0.816)
• Bachelor or Honours degree	-1.435** (0.597)	-0.894* (.537)
• Advanced diploma	-0.966 (0.721)	-0.911 (0.663)
• Certificate III or IV	-0.828* (0.451)	-0.828 (0.451)
• Completed year 12	-1.487*** (0.353)	-1.387*** (0.326)
Employed	1.434*** (0.188)	1.178*** (0.176)
Married	1.892*** (0.237)	1.512*** (0.220)
Has children aged 0 to 14 years	0.133 (0.185)	0.183 (0.172)
<b>Individual ethical behaviour index</b>	<b>0.622*** (0.023)</b>	
<b>Individual perception of advantageous behaviour</b>		<b>0.788*** (0.039)</b>
No. of observations (n)	64,491	68,100

Source: Deloitte Access Economics modelling.

Note: \*\*\*, \*\*, \* indicate statistical significance at the 1%, 5% and 10% level, respectively.

**A.2.2. Ethical behaviour and individual labour market outcomes**

Table A.4 reports the estimated regression results where the dependent variable is an individual’s likelihood of employment. Results are presented in terms of logit coefficients and so cannot be directly interpreted as a change in the probability of employment. The results indicate that there was no statistically significant relationship between the regional ethical behaviour index and employment outcomes but a positive and significant relationship between the regional index assessing whether or not people take advantage of you and employment outcomes.

**Table A.4: Estimated regression results for employment**

Dependent Variable:	Logarithm of wages			
Model specification:	OLS model with RE	OLS model with FE	OLS model with RE	OLS model with FE
Age	0.027*** (0.002)	0.053*** (0.004)	0.028*** (0.002)	0.052*** (0.003)
Age <sup>2</sup>	-0.0004*** (0.000)	-0.0004*** (0.000)	-0.004*** (0.000)	-0.0004*** (0.000)
Gender (male)	0.095*** (0.007)		0.094*** (0.007)	
Education				
• Post-graduate qualification	0.498*** (0.171)	0.085** (0.042)	0.481*** (0.017)	0.086** (0.037)
• Graduate diploma	0.443*** (0.016)	0.120*** (0.039)	0.427*** (0.015)	0.110*** (0.035)
• Bachelor or Honours degree	0.367*** (0.012)	0.022 (0.034)	0.353*** (0.012)	0.015 (0.030)
• Advanced diploma	0.203*** (0.014)	0.020 (0.033)	0.198*** (0.014)	0.017 (0.030)
• Certificate III or IV	0.110*** (0.011)	0.016 (0.024)	0.105*** (0.010)	0.003 (0.021)
• Completed year 12	0.134*** (0.012)	-0.043 (0.031)	0.135*** (0.012)	-0.037 (0.028)
Experience	0.009*** (0.001)	0.001 (0.002)	0.008*** (0.001)	0.002 (0.002)
Married	0.053*** (0.006)	0.023*** (0.009)	0.048*** (0.006)	0.022*** (0.007)
Has children aged 0 to 14 years	0.024*** (0.005)	0.016** (0.006)	0.023*** (0.005)	0.015*** (0.006)
<b>Regional ethical behaviour index</b>	<b>0.023** (0.011)</b>	<b>0.055*** (0.015)</b>		
<b>Regional perception of advantageous behaviour</b>			<b>0.054*** (0.023)</b>	<b>0.130*** (0.017)</b>
No. of observations (n)	37,504	37,504	43,879	43,879

Source: Deloitte Access Economics modelling.

Note: The sample across all model specifications was restricted to people aged between 21 and 65. \*\*\*, \*\*, \* indicate statistical significance at the 1%, 5% and 10% level, respectively. In all models with random effects, wave dummies were additionally included. The results for these dummies, however, are not reported for brevity.

# Appendix B: Modelling the business benefits of ethical behaviour

This section outlines the econometric techniques used to examine the association between measures of ethical behaviour at an organisation level and financial performance.

As noted in 3.2.2 above, the analysis was performed using data from two sources. To obtain a measure of the perception of a firm's ethics, we used the Governance scores from the RepTrak Company's Reputation Index over the period 2009-2020. For some companies this is recorded at two points during a year and in these cases, the Governance scores were calculated as an average of these two observations for that financial year. This index was then matched to annual financial performance data from IBISWorld. After excluding observations in which the return on assets exceeded 200% which were deemed to constitute outliers, this resulted in a total of 338 remaining observations across 49 companies.

The key outcome considered was a firm's Return on Asset (RoA).<sup>71</sup> RoA is likely to provide a better measure of a firm's financial performance as it controls for differences in the size of the asset base between companies.

## B.1. Methodology

The association between governance scores and financial performance was examined through the following autoregressive time series model:

$$RoA_{i,t} = Governance\ score_{i,t} + RoA_{i,t-1} + a_i + IND_i + u_t + \varepsilon_{i,t}$$

where firm  $i$ 's ROA in year  $t$  is a function of its ROA in the last period (i.e. year  $t-1$ ), its Governance score in year  $t$ ,  $a_i$  is a time-invariant company variable capturing company fixed effects,  $IND_i$  is a set of industry controls,  $u_t$  captures year fixed effects to account for differences in economic conditions over time and  $\varepsilon_{i,t}$  is a normally distributed error term.

The specification of the model is also known as the lagged dependent variable model, because the lag of the dependent variable, ROA, enters the model as a predictor in the right hand side of the equation. The inclusion of the lagged ROA controls for the firm's financial performance in the previous year.

The inclusion of a company fixed effect similarly controls for the extent to which an individual companies typically achieves stronger or weaker ROA outcomes relative to what would be predicted by its past financial performance. This company fixed effect is likely to capture a range of features of an individual company which may cause it to have relatively high or low return on assets (after accounting for return on assets in the previous year) including factors such as brand, culture and management quality.

Given these controls, the equation is examining the degree to which variation in a firm's governance score is associated with return on assets, controlling for past return on assets and the extent to which the firm typically achieves higher or lower return on assets relative to what would be predicted by the model.

Return on assets was selected as an appropriate measure of business success because it incorporates debt and equity assets. Therefore, it is more comprehensive than the usual measure of investment return, which is Return on Equity (ROE). ROA data was also more widely available, ensuring a large sample could be used in the analysis.

## B.2. Causality

While the analysis controls for past financial performance – both return on assets and company specific performance - in theory it is possible that reverse causality may be present. This is an issues that has been identified in much of the empirical literature in this area. That is, return on assets this year could also influence governance scores this year. For example, it is possible that firms that do well in a given year may be more willing to be fair in their dealings with customers and other businesses. This is certainly possible but it could also be argued that decisions to improve ethical behaviour are more likely to be made by the management of a business if they also believe it will also lead to improved financial performance rather than simply once a certain threshold of financial performance has been achieved. It is also worth noting that measures of the Governance Index are captured earlier in the year than full financial year results.

## B.3. Results

Table B.1 sets out detailed regression results using both RepTrak's Governance Index and Pulse Index. The latter captures broader components of a business' reputation beyond governance.

**Table B.1 Perception of company ethics and Return on Asset (RoA) modelling results**

Dependent variable:	Return on Assets	Return on Assets
RepTrak Governance Index	0.010* (0.006)	
RepTrak Pulse Index		0.016*** (0.006)
Lagged Return on Asset	0.067 (0.046)	0.065 (0.045)
Construction	0.156 (0.242)	0.137 (0.238)
Electricity, Gas, Water and Waste Services	-0.346*** (0.174)	-0.313* (0.171)
Financial and insurance services	-0.434*** (0.182)	-0.406** (0.173)
Information, Media and Telecommunications	-0.792*** (0.179)	-0.695*** (0.178)
Manufacturing	-0.596*** (0.201)	-0.691*** (0.202)
Mining	-0.214 (0.174)	-0.190 (0.171)
Retail Trade	-0.308 (0.184)	-0.362** (0.182)
Transport, postal and warehousing	-0.532*** (0.194)	-0.590*** (0.191)
Wholesale Trade	-0.010 (0.185)	-0.005 (0.183)
Constant	-0.014 (0.34)	-0.375 (0.377)
Year fixed effects	Yes	Yes
Company fixed effects	Yes	Yes
No. of observations	338	338
R <sup>2</sup>	0.458	0.465

Source: Deloitte Access Economics (2020) modelling. Note: \*, \*\*, \*\*\* mean statistically significant at the 10%, 5% and 1% level respectively. Results for company and year fixed effects are not presented here for brevity.



# Appendix C: Modelling trust and economic outcomes

There is an extensive economic literature examine the relationship between trust and economic outcomes, much of which draws on cross-country regression modelling to examine whether countries with higher levels of trust (or other measures of social capital) have higher income levels.

A seminal paper by Knack and Keefer (1997) examined the relationship between trust (and also other measures of civic behaviour) on economic growth between 1980 and 1992 using the World Values Survey.<sup>72</sup> Trust was measured in 1980 to avoid the potential for endogeneity in the relationship between trust and economic growth, as using trust and economic growth from the same year makes it difficult to entangle whether trust is leading to greater economic growth or economic growth is creating greater levels of trust.

Knack and Keefer, in particular note that trust is likely to affect economic growth through increasing total factor productivity and capital and labour accumulation. They show that that relationship between trust and economic growth is no longer significant once investment share of GDP is controlled for – arguing that capital accumulation is a way in which trust improves economic outcomes. This implies that including variables reflecting capital accumulation in the analysis may understate the impact between trust and GDP as improved trust is likely to impact the level of investment in physical. They note similar concerns in relation to human capital accumulation and use measures of primary and secondary enrolment in 1960 in their primary specification. The inclusion of more contemporary measures of human capital accumulation could indirectly capture the degree to which trust impacts GDP through human capital accumulation and they find some evidence of this effect with alternative measures.

Algan and Cahuc (2013) build on these findings by adopting a similar approach but extending the period of analysis of economic growth to 1990 to 2009 also drawing on data from the European Values Survey.<sup>73</sup> Algan and Cahuc (2010) make another important contribution to this literature by using an alternative approach to estimate the causal relationship between trust and economic growth.<sup>74</sup> They proxy trust based on measures of inherited trust among respondents in the US to the General Social Survey. More specifically they track changes in trust levels inherited by different generations of Americans from the countries of their immigrant forebears to capture the evolution of trust in source countries. This allows the authors to isolate the impact of trust on economic development independently from contemporary economic performance. The authors find that trust has a significant impact on economic development.

## C.1. Data

The analysis draws on measures of trust captured in the European Values Survey and World Value Survey. The World Values Survey (WVS) contains a collection of nationally representative surveys conducted across almost 100 countries covering nearly 90 per cent of the world's population.<sup>75</sup> The World Values Survey was matched with data from the European Values Survey which has additional measures of trust for a range of European countries.

The World Values Survey has six waves of data and this was matched to measures of GDP and a range of other control variables.

## C.2. Methodology

The methodology used was broadly similar to that proposed by Knack and Keefer (1997) and Algan and Cahuc (2013). The analysis considered the impact on a lagged measure of trust (the average proportion who indicated most people can be trusted between 1980 and 1990) and GDP per capita. The key control variables included in the analysis were:

- Human capital based on the index of human capital per person from the Penn World Tables based on average years of schooling and assumed rates of return on education.<sup>76</sup> The average value of this variable between 1980 and 1990 was used.
- The Index of Economic Freedom- an annual index that seeks to measure the degree of economic freedom across countries capturing a range of measures in relation to the strength of the rule of law, size of government, regulatory efficiency (business, labour and market freedom) and the degree of market openness. The index ranges from 0 to 100.
- A country's population.
- The price of investment goods captured by the price level of the share of output-based gross domestic product that is represented by capital formation (investment) from the Penn World Tables relative to the price level of output based GDP in the US.
- Polity V index which measures the strength of democracy in a country based on an evaluation of competitiveness of elections, openness, political participation and checks on executive authority. The index is measured on a range from -10 to 10.

The key results are set out below Table C.1 below. The first column reports results using contemporaneous measures of trust and includes country and year fixed effects. The second and third columns report reports using a lagged measure of trust. The estimates of the impact of GDP is based on the coefficient on lagged trust in the final column where lagged trust is used to address the potential endogeneity between trust and GDP.

**Table C.1 The relationship between trust and GDP per capita**

<b>Dependent variable:</b>	<b>GDP per capita</b>	<b>GDP per capita</b>	<b>GDP per capita</b>
Log (General Trust)	4125.03* (2195.50)		
Log (Lagged General Trust 1980-1990)		12612.67*** (4224.34)	10873.97** (4232.81)
Economic Freedom Index	852.29*** (145.75)	539.78*** (191.89)	674.56*** (188.16)
Population	15.02 (32.30)	16.31** (6.48)	20.003** (6.26)
Price of investment goods	2931.71*** (1091.59)	68551.14*** (6365.07)	73410.69*** (5437.36)
Polity V index	34.87 (79.96)	1898.27*** (466.46)	1827.38*** (465.15)
Lagged Human Capital		8831.27** (3638.62)	7186.17** (3495.26)
Constant			-8691.77*** (15021)
Year fixed effects	Yes	Yes	No
Country fixed effects	Yes	No	No
No. of observations	244	126	126
R2	0.2276	0.8213	0.8334

Source: Deloitte Access Economics (2020) modelling. Note: \*, \*\*, \*\*\* mean statistically significant at the 10%, 5% and 1% level respectively. Results for country and year fixed effects are not presented here for brevity.

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49. The RepTrak Company uses the IBISWorld Top 2,000 Company list to determine the 60 largest companies by revenue each year.
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61. These skills are outlined on the Federation of Australasian Philosophy in Schools Associations website. <<https://fapsa.org.au/curriculum/national-curriculum/>>
62. The success of Primary Ethics in public primary schools in NSW can serve as a model for other states.
63. As of August 2020, philosophy is a subject in Victoria and Western Australia's high school leaving exams, and in the International Baccalaureate curriculum.
64. Research suggests that ethics courses in university are most impactful on students when they are integrated into other coursework, rather than as standalone ethics units (Damon, 1997). This leads young people to more likely see them as valid and draw connections to other areas of study and life, rather than as context specific.
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