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The Decay of Ethical Discernment: The Importance of Inspiration

Any meaningful, positive change in the ethical conduct of our industry can only come about if you are willing to accept a greater leadership and stewardship role.

BY DONALD B. TRONE

For a number of years, magazine editors have approached me with requests to write a column on ethics. Until now, I have politely refused because I have never considered the subject to be foundational to my research on fiduciary responsibility, nor have I ever wanted to be labeled as an ethereal ethicist — an "ethics cowboy" who is all hat and no cattle.

The events of the past six years have caused me to spend more and more time augmenting my research on fiduciary responsibility with stories on leadership, stewardship, character and integrity. A cornerstone to all these subjects is ethics — or at least it should be. Unfortunately, I am discovering more instances of unethical behavior and finding that these ethical breaches are being masked by legal devices or hidden by obtuse regulations. A person's word; a firm handshake; an agreement in principle; even contracts and agreements no longer seem to matter — what matters is what legal counsel can help you get away with.

What we are witnessing is the decay of ethical discernment.

When I first entered the industry 26 years ago, experienced professionals all shared the same advice — *your reputation is everything; don't do anything to soil it.* Sadly, this no longer is the case. In some circles a reputation for unethical behavior, or even a willingness to be unethical, is considered a plus. Reputation is no longer sacred; today it is just another expendable asset — as expendable as long-term employees and loyal customers. Consider the following:

- When SAC Capital Advisors was hit with charges of insider trading, it actually witnessed net inflows of $1.6 billion.

- In 2012, a survey of 500 professionals by the law firm of Labaton Sucharow revealed that 30% of the respondents felt that their compensation or bonus plan created pressure to compromise ethical standards.
- In 2012, Ernst & Young conducted a survey of 400 CFOs; 47% responded that they could justify unethical practices if it could be demonstrated that it would help their organization survive the current economic downturn.

The same can be said about the typical code of ethics — most are now codes of *conduct*. A code of ethics is based on principles; a code of conduct is based on rules. When a code begins with the words, "Thou shall not…", then it's a code of conduct, not a code of ethics. The advantage of a code of conduct is that you don't have to think — you don't have to judge wisely and objectively — you just have to follow the rules. And when the rules become a problem, you often can find ways to bend them with a legal device, such as using a dense disclaimer filled with legalese to cover up a conflict of interest.

THE POINT OF INSPIRATION

What's the difference between motivation and inspiration? Are people in the financial services industry motivated or inspired? Often the words are used interchangeably, but that's a mistake, particularly as it relates to ethics.

> *Motivation is something we do to other people. When we motivate people, we are attempting to control their behavior; often to serve our own purposes, not theirs. Motivation always comes with a price: When it is about "me" at the expense of "you," the result is often resentment, lack of trust and reprisal. — Lance Secretan, author of* The Spark, The Flame and The Torch

Our industry is motivated by fear, greed and ego — we reward the sale of a product or the gathering of assets, but we do not reward stewardship. We send people off to leadership conferences because of their revenue production, not because they are genuine leaders.

A restoration of ethical discernment can only come about through inspiration — which is the opposite of motivation. The fallacy of the Dodd-Frank Act, and similar legislation and regulations which are meant to restore the public's trust, is that more rules will never translate to better ethical behavior. Never in the history of civilization has imposing more rules improved the character of citizens. If ethics is the cornerstone to leadership, stewardship, character and integrity, then inspiration is the keystone.

For example, how inspiring is 408(b)(2)? Everyone was expecting that 408(b)(2) would be a game changer; that we would see an asset flow tsunami as plan sponsors considered the impact that fees and expenses had on their plan. Instead, there has been barely a ripple. The regulations, which were intended to bring greater transparency to the industry and, in turn, provide a wider view of potential conflicts of interest, have not had a meaningful, positive impact on the industry. The reason: There's nothing inspiring about 408(b)(2).

Consider also the PBS Frontline program, "The Retirement Gamble." Much has been written about the program, so I'm only going to add my thread as it relates to this column. What the producers missed is that this is a crisis in leadership and stewardship. Excessive fees and the lack of uniform professional standards are the symptoms; the disease is the lack of inspiration.

Start with participants — they have been poor stewards of their retirement assets. Why? Because they haven't been inspired to save more. Participants cannot be expected to rise above the level of enthusiasm or engagement of the plan sponsor. Leadership flows from the top down. If an organization does not inspire greatness, it will not have a great plan. If participants perceive management as being uncaring, they are not going to have a great deal of faith in the retirement plan. If leaders don't care, you can bet their followers won't either.

Speaking at a Retirement Advisor University session at UCLA in early May, I made the comment that advisors should suggest to plan sponsors that rank and file employees should be permitted to serve on the investment committee. One of the advisors immediately shot up her hand and said, *"But most plan sponsors don't trust their employees to provide meaningful feedback on the plan."* My point exactly — if a sponsor doesn't trust or respect their employees, there isn't a snowball's chance of finding a point of inspiration.

Legal devices and obtuse regulations have become the prosthesis for what we once considered ethical discernment. Ethics has been displaced with a check-box mentality — if you can find reason to check the box, it must be okay.

Any hope of restoring ethical discernment must come from inspiration. Any hope of improving participant outcomes must come from inspiration. And any hope of improving a plan sponsor's procedural prudence must come from inspiration.

Where do we find such points of inspiration? Where do we start? It has to start with you — in the eyes of your clients you have to be the point of inspiration for moral, ethical and prudent decision-making. Any meaningful, positive change in the ethical conduct of our industry can only come about if you are willing to accept a greater leadership and stewardship role. PC

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