

Codes of Ethics and the Economic Results of Companies

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Abstract

The goal of this paper is to determine how widespread the presence of a code of ethics is and the possible relationship between the presence of a code of ethics in Czech companies and the positive economic results of those companies over the last five years. The number of companies that are introducing ethical management continues to grow globally, including in the Czech Republic. A code of ethics is a tool with which to determine the ethical infrastructure of a company, as well as manage it. However, expert opinions on the possible economic impact of ethical management differ considerably. A statistical analysis of the results obtained from a questionnaire survey conducted among a sample of 297 companies showed that the presence of a code of ethics, or a lack thereof, has no demonstrable impact on the economic results of a company regardless of its size.

Keywords: Code of ethics, economic impact, prosperity, management, company, ethical.

Introduction

A code of ethics is the basic, traditional and most widely used tool for the ethical management of a company (Farrell, Cobbin and Farrell, 2002). According to Caha and Urban (2017), the advantages of having a code of ethics are that it: modifies behaviour by providing possible instructions and examples of how to behave; solves conflict situations; defines acceptable and unacceptable behaviours thereby clarifying company policy; positively influences employee's awareness of their sense of place and identity with regards to the company, and of the support they receive (codes of ethics force employees to think about their roles and obligations towards the company and/or its customers, whilst making employees feel safe and protected); improves a company's reputation with its customers and the general public; helps solve disputable questions with regards to the introduction of innovations; keeps managers in check by preventing them from abusing their positions in relation to other employees; helps to reveal illegal activities and transactions; prevents superiors from requiring subordinates to behave inappropriately. Mazák (2010) states similar reasons for organisations to create and apply a code of ethics:

it defines the limits of desirable behaviour for company employees as well as entities outside the organisation; it eases decision making by unambiguously specifying company principles; it may be a criterion on which basis an organisation can be assessed externally; it is an undertaking to adhere to a set of principles which improves the credibility of a company. It should be noted at this point that codes of ethics are not strict rules and laws, but only manuals, which can also work counterproductively if undue pressure is brought to bear on organisations and employees to apply them. A code of ethics does not therefore only represent a tool of management or autoregulation within an organisation, it also contributes to improving the credibility of a particular entity in the eyes of its stakeholders.

The importance of a code of ethics in current company practice is also related to its capacity to strengthen a company's ability to manage information (Weller 1988). Examples of ethical questions that might arise are: What can managers expect from the employees with regards to the non-disclosure of confidential information if an employee decides to leave a company and start working elsewhere? What information is owned by a company and what know-how is owned by an employee? Should an employee know that their activities will be monitored under certain circumstances? Does the collection of data on an employee violate their right to privacy? Should systems liable to a breach of data protection be controlled? What are the responsibilities of a manager and an organisation with regards to data protection? Another problem within this context is the increasing use of social networks by employees for communication purposes, both on company profiles and on private accounts.

Companies are increasingly becoming aware of the fact that improper communications through social media can have serious consequences for their reputation and their image in the eyes of the general public. In fact, a digital footprint is permanent. There are therefore fully legitimate reasons why companies are stepping up their efforts to set principles and rules for employees with regards to such communications. At present, two models are being applied in practice: a company prepares a special document containing adjustments to the rules of communication with regards to social networks; or a company integrates new rules on communications on social networks for their employees into an existing code of ethics. Irrespective of which model a company decides to apply, it is imperative that they act promptly and do not postpone implementing effective measures. Failure to do so may result in numerous labour disputes.

Globalisation and the existence of global companies also raises numerous issues with regards to the preparation of global codes of ethics. This is primarily due to intercultural differences in business ethics on how to effectively solve ethical dilemmas. This therefore requires the building of a consensus around the setting up of "global standards" (McLeod, Payne and Everet, 2016).

According to Caha and Urban (2017b), the key instruments of ethical management, to which codes of ethics belong, are:

Ethical leadership - leading by example every day throughout working hours. The behaviour of company officials should conform with each other. Potentially unethical behaviour by company management leads to the degradation of the ethical behaviour of its employees. Low cost and authenticity, or genuineness and credibility in the approach to business ethics are some of the advantages of ethical leadership as an organisational management tool. It is also gives a clear signal about the credibility of the ethical declarations of an organisation.

Use of whistleblowing - this means the active notification of a particular unfair practice that takes place within the workplace. Employees are usually among the first to learn about unfair practices and can point them out. An employee may however face various dilemmas in such a situation, in particular with regards to the question of whether they should be disloyal to their colleague(s), line manager or employer, thereby putting their own position at risk, or whether it is more important to protect the public interest. Whistleblowing therefore requires an arrangement to be in place, usually integrated in an organisation's code of ethics, which includes an undertaking not to sanction in any way the person that provides the information on the unethical behaviour. Whistleblowing is therefore one of the most important tools for making disclosures and preventing fraudulent and corruptive practices in public administration and in private companies. Such disclosures can lead to the saving or recovery of substantial public funds, and prevent the loss of life. The contribution of whistleblowers to the prevention of corruption is undisputable, however the credibility of the policy depends wholly on the precondition that no sanctions are imposed on or retaliatory measures taken against the person making the disclosure. The credibility of this tool is therefore higher if the code of ethics of an organisation contains guarantees that the organisation supports an environment in which employees are not afraid to report potential fears and problems, that it does not tolerate any kind of retaliatory measures against anyone who in good faith reports an alleged breach of obligations or provides any information in relation to an investigation of an alleged breach. These guarantees should also ensure that the organisation will investigate all cases of potential retaliatory measures taken against anyone who reports incorrect behaviour and punish those employees that do so.

Education and training of employees and managers – education in the field of ethical behaviour should unify the opinions of all employees on the importance of ethics in everyday work and teach effective communication supporting openness and confidence inside a company. The following is an example of ethical management within a construction company and the consistent application of the tool. The construction company decided that all new employees must attend training on the principles that govern the company's code of ethics and the observance thereof, no later than three months after the commencement of their employment. Furthermore, all the employees should be trained in ethical behaviour at least once every two years. The company maintains exact records on the completed training sessions, including lists of the employees who participated. After each course the employees must confirm that they

attended the course, that they understand the code of ethics and that they agree that they will behave in an appropriate way within their activities as employees of the company.

Reporting the risk of a breach of ethics rules - this practice pursues similar goals to whistleblowing, but does so in a slightly different way. It is based on the obligation of managers and employees to provide the line manager or an appointed company officer with timely and relevant information about a situation in which there is a risk of a breach of the ethics rules. The reporting of such situations can be combined with a preliminary risk assessment and accompanying action plan. Such situations include events which might either tarnish the brand name of the company (business ethics, the environment, safety, health), or lead to a breach of legal obligations e.g. a deadly injury or another serious accident, pollution of the environment, serious environmental accident, etc.

Internal ethics committee – such committees are subordinate to an organisation's management and consist of its managers and employees. It usually includes the company lawyer, human resource manager and an experienced operational manager. The areas of responsibility of an ethics committee include the provision of counsel on ethics issues, the investigation of alleged breaches of the code of ethics, and the making of recommendations to management.

Ethics audit – this is a systematic evaluation of the ethics programme within a company and the verification of its ethical standards.

Corporate social responsibility, corporate governance and compliance management – the code of ethics of an organisation is closely related to other management tools which include ethics, in particular those systems and tools utilised to implement a company's strategies with regards to corporate social responsibility, corporate governance and compliance management (the system for monitoring and assessing whether a company adheres to certain internal and external rules regarding its business operations). In some cases the sources for the code of ethics also include the concept of the sustainable development of society or of a particular company.

Codes of ethics form a systemic framework for a company's ethical infrastructure and for the application of an integrated system of ethical management (Seknička and Putnová, 2016). The term "code of ethics" (code of conduct) is understood to be a clearly elaborated set of standards and regulations that defines and modifies relations between members of a certain community (Rolný, 2007).

A code of ethics defines in detail the moral principles of a company and their application to company practice (Murphy, 1998). The purpose of a code of ethics and similar documents is to cultivate a particular company environment and culture. According to Remišová (2011), a code of ethics should not be perceived as a legal document. In fact, a code by its very definition points out the intention to behave ethically in all the above mentioned aspects and to respect the current social and legal standards. A code of ethics should be comprehensible, communicable, specific, up-to-date and enforceable.

According to Ho (2010), a code of ethics only has a positive influence on the ethical behaviour of employees if it is presented in the right and appropriate way. Numerous factors play an important role in this process, including the overall orientation of the company, an employees' field of work, etc. Singh (2011), for example, recommends that codes of ethics should be evaluated and revised every two years, whereby all company employees should be informed of any changes during a training session. New employees should also be familiarised with the code of ethics, namely prior to the commencement of their employment.

However, codes of ethics are also subject to criticism. Their poor efficacy, poor enforceability, formalism and high level of generality are particularly reproached, as is the fact that the behaviour of individuals is more or less determined by the values they acquire during childhood (Putnová and Seknička, 2007). The question as to what extent a code of ethics is useful for small companies and small entrepreneurs with a fixed organisational culture that works mainly on the basis of informal relations, is also disputable (Čaník and Čaníková, 2006). Some companies may see the only advantage of creating a code of ethics as the improvement in their image in the eyes of customers and the general public. The fact that employees do not know the code of ethics well enough, which leads to its violation, is another problem (Ho, 2010).

A code of ethics is also not necessarily accompanied by an improvement in company ethics. Several empirical studies have revealed that codes of ethics give companies a negligible advantage, if any advantage at all. Research conducted by McKendall, DeMarr and Jones-Ridders (2002) is an example of one of these studies. In their research, Kaptein and Schwartz (2008) also concluded that the efficacy of codes of ethics was relatively low. Nevertheless, despite the mixed results of studies into the efficacy of codes of ethics in companies, it is possible to observe that well-functioning codes provide a high potential for improvements in overall business and company culture. Čaha and Urban (2017b) deal with the main principles of the contents, creation and enforcement of codes of ethics in organisations, the extent to which this management tool is used by Czech companies, including differences in its usage in different types of organisations, the frequency of its evaluation and subsequently make suggestions for changes.

A global survey conducted by KPMG (2008) points to the worldwide trend for increasing numbers of companies to define and implement a code of ethics. The research showed that in 2008 the proportion of companies with a code of ethics stood at 86%. It is clear from the above that in recent years a code of ethics has become a standard basic tool for ethics programmes within large and renowned companies. This is also backed up by an informal survey conducted by IBE in 2012, which showed that a code of ethics was implemented by 92% of those companies with the highest market capitalisation based in Great Britain whose shares are traded on the London Stock Exchange (IBE, 2012). The IBE survey also reported that in 2012, 73% of all companies had a code of ethics. The CGMA (2015) conducted a survey the overall results of which showed that the proportion of companies with a code of ethics stood at 82% (and among large companies 93%). In 2016, according to a worldwide survey conducted by PwC, the largest of its kind, in which 6,337

companies from 115 countries participated (including 79 prominent companies from the Czech Republic), revealed that on average 82% of companies had a formally established code of ethics (PricewaterhouseCoopers, 2016).

One of the latest surveys was conducted in 2016 by Dow Jones and Metricstream (2016) and showed that 96% of the 330 questioned companies had a code of ethics. The aforementioned surveys indicate the growing trend towards the introduction of codes of ethics in business practice. However, it is important to highlight that not all these surveys are compatible. In reality, the results depend on numerous factors, in particular on the structure of the respondents. Whilst a higher proportion of large US based companies have codes of ethics, this proportion is smaller for small and medium-sized companies and companies operating in Asia. It is clear that only global surveys with large numbers of respondents from all business sectors and companies of different sizes will therefore provide the relevant information required. Unfortunately, such surveys are difficult to realise.

According to a survey conducted by the Association of Chartered Certified Accountants (ACCA), one in five managers or accountants in the Czech Republic has had to deal with a serious ethical dilemma in their work. This only confirms the necessity of introducing effective ethical management tools (Transparency International – Czech Republic 2015). Džbánková (2003) concluded, on the basis of her smaller less representative survey conducted in 2002, in which 60 representatives participated from middle and top management in companies operating in Prague and Central Bohemia, that 35% of the questioned companies had a code of ethics in place and 22% were considering drafting and implementing one. In contrast, Transparency International – Czech Republic, in conjunction with the Economic University in Prague, conducted a very representative survey in 2005, which was repeated in 2006. The surveys sought to determine the degree to which codes of ethics were applied in companies that operated on the Czech market. The conclusion was that in the second half of 2005 only 59 companies (i.e. 10.3%) of the 574 questioned had a code of ethics in place. This situation was similar when the survey was repeated in the first half of 2006, whereby only 104 companies (i.e. 8.4%) of the 1,240 in the sample set had a code of ethics in place. The survey also proved that the larger the company the greater the chance a code of ethics existed. Dytrt et al. (2011) state that in 2011, less than 15% of domestic companies had a code of ethics in place. In a more recent survey conducted by Transparency International in 2013, the results showed that this percentage had increased to 46% of domestic companies. However, this compares to the world average of 74% (Transparency International – Czech Republic 2015). According to the respondents of a questionnaire survey conducted in 2015, the results of which were processed by the Financial and Economic Institute, 68% of companies had a code of ethics, but only 23% of companies saw the code of ethics as a binding set of rules (Finanční a ekonomický institut, 2015). According to the previously mentioned PwC survey, in which 6,337 organisations from 115 countries participated, 86% of the 79 prominent Czech companies questioned had a formally established code of ethics. However, the low

number and the size of the companies involved belies reality (Global Economic Crime Survey 2016 – Report for the Czech Republic 2016).

Despite these results, the number of companies in the Czech Republic that are establishing a code of ethics is gradually growing, although the numbers remain well below the global average (which is higher than 70%). In the Czech Republic, the presence of a code of ethics tends to be limited to larger companies and public institutions. Smaller companies are still only exploring their options with regards to this ethical management tool.

The application of ethical management principles is a long-term intention, which does not usually lead to an immediate effect. When creating a code of ethics a company must take into account that significant efforts will be required to make the staff understand the principles maintained therein (Erwin, 2011). In some cases, having to deal with ethical issues may generate unwillingness among some employees to cooperate. Under such circumstances it is necessary to create a motivational system which encourages the involvement of employees in the creation and the application of a code of ethics.

Materials and Methods

In order to fulfil the set goal of the contribution, quantitative research was carried out on the basis of an electronic questionnaire survey conducted between June 2016 and August 2016. The aim of the survey was to obtain a statistically representative cross-sectional data set on small, medium-sized and large companies. In total, questionnaires were sent/given to 710 targeted companies selected from random industries. In total, 297 responses were received, which is equivalent to a response rate of 41.83%. The analysis of the survey results set out to verify the hypothesis that the presence of a code of ethics in a company has no influence on its economic prosperity. Unfortunately, the representativeness of the data is limited because the analysis only focuses on three categories of company size (see Table 1). The differences between the categories of company size are evaluated using the standard, unpaired, two-tailed statistical Chi-square test of relative frequency differences. R statistical software was used for the relationship tests and the calculation of the interval estimates. All the statistical tests and calculations of interval estimates were performed at a confidence level of 95% (i.e. at a significance level of 0.05).

The initial survey was subsequently followed up with a second electronic questionnaire, the results of which are not included in this paper due to ongoing data processing. The second data set will be used to analyse companies in more detail at a later date.

Table 1. Absolute numbers and relative frequencies according to company size

Company size	Number	Frequency in %
Small/micro-companies	110	37.0%
Medium-sized companies	103	34.7%
Large companies	84	28.3%
Total	297	100.0%

Source: Author

It is important to note at this point that there is a potential systemic and confounding bias in the design of the survey because the outcome of the categorical variable is self-evaluated. Another issue is the overrepresentation of active companies because failing companies are less likely and willing to provide true information. In response to this, further research will be conducted into the financial situation of companies. In this way, more precise differences between various categories of companies can be analysed.

For the analysis, three categories of companies were identified, namely large companies (≥ 250 employees), medium-sized companies (50 – 249 employees), and small and micro-companies (< 50 employees). The purpose of the analysis was to determine how widespread the presence of a code of ethics is and the possible relationship between the presence of a code of ethics in Czech companies and the positive economic results of those companies over the last five years. Within the sample dataset, there were several companies that gave no response to the question “Does your company have a code of ethics?” It was decided to assign the answer “No, we do not miss it” to these cases on the basis of the assumption that omitting to answer the question automatically shows that the company does not have a code of ethics. In addition, our interest was only in whether a company does or does not have a code of ethics. As a result, it was decided, for this analysis, to combine the number of responses for “No, we do not miss it” and “No, we miss it” into one group “No”.

As part of the analysis of the relationship between the presence of a code of ethics and a company’s profit or loss, it was necessary to discount five companies which failed to declare whether their economic results were positive, balanced or negative. In these cases, it was not possible to automatically assign any other option.

Results

Table 2. Presence of a code of ethics according to company size

	Does the company have a code of ethics?	
	Yes (no.)/frequency (%)	No (no.)/frequency (%)
Small/micro-companies	15 13.6%	95 86.4%
Medium-sized companies	31 30.1%	72 69.9%
Large companies	54 64.3%	30 35.7%
Total	100 100.0%	197 100.0%

Source: Author

The testing of the hypothesis: “*The presence of a code of ethics has no impact on the economic results of a company*”, was conducted separately for each category of company size. The proportions for the profitable companies are highlighted in bold in the relevant tables. A two-selection test was subsequently carried out on the identity of the two proportions to determine whether the statistical difference in the proportions for profitable companies was dependent on the presence of or lack of a code of ethics.

Table 3. Code of ethics in large companies and economic results

Code of ethics	Economic results			Two-selection test	
	Balanced	Positive	Negative	Z - test	0.8499
Yes	0.130	0.796	0.074	p - value	0.3954
No	0.133	0.867	0.000	Interval	(-0.0919; 0.2327)

Source: Author

Note: 84 observations

As the p-value is higher than the significance level of 0.05, the test shows that the difference in the proportion of profitable companies in the group with or without a code of ethics is statistically insignificant. The presence of a code of ethics therefore does not affect the economic results of large companies (see Table 3).

Table 4. Code of ethics in medium-sized companies and economic results

Code of ethics	Economic results			Two-selection test	
	Balanced	Positive	Negative	Z - test	0.2233
Yes	0.226	0.742	0.032	p - value	0.8232
No	0.162	0.721	0.118	Interval	(-0.2087; 0.1660)

Source: Author

Note: 99 observations

The p-value is once again higher than the significance level of 0.05. The difference in the proportion of profitable companies in the group with or without a code of ethics is also statistically insignificant. The presence of a code of ethics therefore does not affect the economic results of medium-sized companies either (see Table 4).

Table 5. Code of ethics in small/micro-companies and economic results

Code of ethics	Economic results			Two-selection test	
	Balanced	Positive	Negative	Z - test	0.3881
Yes	0.267	0.600	0.133	p - value	0.6979
No	0.274	0.652	0.074	Interval	(-0.2131; 0.3184)

Source: Author

Note: 110 observations

In this case, the p-value is also higher than the significance level of 0.05. Once again, the difference in the proportion of profitable companies in the group with or without a code of ethics is statistically insignificant. The presence of a code of ethics therefore does not affect the economic results of small/micro-companies either (see Table 5).

Discussion

Even though the results of the research showed that the presence of a code of ethics has no demonstrable impact on the economic results of a company, this has not discouraged or hindered the increasing trend for companies to introduce ethical management, which

reflects the positive impact companies believe it brings to their company culture and public image.

Further research should focus on the differences between groups of companies based on technical efficiency, labour productivity, research and development expenditures, and profitability. Also MANOVA would shed some light on the potential relationships between economic results, company size and the presence of a code of ethics. Non-financial performance variables like employee satisfaction should also be taken into consideration. These variables can contribute to a better understanding of the total performance evaluation of ethical culture within companies.

Conclusion

The goal of this paper was to determine how widespread the presence of a code of ethics is and the possible relationship between the presence of a code of ethics in Czech companies and the positive economic results of those companies over the last five years. The aim of the electronic questionnaire survey that was conducted to achieve this goal was to obtain a statistically representative cross-sectional data set on small, medium-sized and large companies. The testing of the hypothesis: "The presence of a code of ethics has no impact on the economic results of a company", was conducted separately for each category of company size. The statistical tests performed on the basis of the results of the questionnaire survey showed that the presence of or lack of a code of ethics has no demonstrable influence on the economic results of a company, irrespective of their size.

Nevertheless, the conducted research is unique and involves a relatively large sample set which introduces new findings to the field of ethical management.

Despite the results of this study, it is possible to claim that well-functioning codes provide a high potential for improvements in overall business and company culture.

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