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# Organizations Gone Wild:

## *The Causes, Processes, and Consequences of Organizational Misconduct*

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**Abstract**

Although research on organizational misconduct has a long history and a recent increase in popularity, important questions are still unexplored. We review and critique research on misconduct with an emphasis on organizational causes. In addition to reviewing some active areas of research, we also examine less-trodden areas and make suggestions for their development. We find that the definition of misconduct is often implicit and the role of social-control agents in identifying misconduct has been neglected, suggesting a need for more rigor in how researchers define the boundary of misconduct

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and measure the labeling of misconduct. The spread of misconduct within and among organizations has also seen relatively little attention, as has the spread of the consequences of misconduct, suggesting a need to examine diffusion of misconduct. Finally, organizational misconduct has been an effective context for testing theories on themes such as motivation, control, power, labeling, and status, and will continue to be an important research topic for both its applied value and its theoretical import.

## Introduction

"Organizations gone wild" has become a subtext of many headlines in the general press and business press. Although research often lags behind the news cycle, the phenomenon has existed long enough that there are scholarly investigations on misconduct toward owners such as deceptive accounting (Harris & Bromiley, 2007; Krishnan, 2005) and option backdating (Lie, 2005), misconduct toward employees such as sweatshops (Rock, 2003), misconduct toward customers such as dangerous products (Govindaraj & Jaggi, 2004), and misconduct toward third parties such as environmental degradation (Alexander & Cohen, 1996; Hoffman, 1999). Indeed, organizational misconduct has a long history in management research (e.g., Staw & Szwajkowski, 1975). Ultimately, it bears on issues of compliance, punishment, and social order that are fundamental in the social sciences (Coleman, 1990; Durkheim, 1984). Management researchers have an interest in misconduct because organizations have become arenas and actors of misconduct with potential consequences that far exceed what individuals are capable of outside the organizational context.

Research on organizational misconduct occurs against the background of a strong set of commonsense intuitions. Put starkly, they are as follows. Acts are labeled as misconduct whenever they are harmful or morally objectionable. They are done by bad people. They occur in organizations that tempt their members too much and control them too little. Discovery of misconduct harms the responsible organization or individual, and leaves others untouched. Although there is some merit in testing these intuitions, research is more valuable when applying new theoretical insights and generating counterintuitive findings. In this paper, we review evidence and develop theory with an eye to finding such surprises. Thus we are particularly interested in how actions may be labeled differently based on the actor or the context. We will ask whether misconduct can be produced by high control and occur in the absence of rewards. We will examine whether perpetrators get away with it and whether innocent actors are harmed.

We structure our discussion around the following issues. First, how should misconduct be defined? Second, what are the causes of misconduct? Third, how does misconduct spread? Fourth, how do behaviors come to be classified as misconduct? Finally, what are the consequences of misconduct? Among these issues, the causes of misconduct are best covered in current research, as multiple individual and organization-level explanations have been proposed. Far less common are (1) a rigorous definition of misconduct, (2) a view of social-control agents as judges that socially construct misconduct, and (3) examination of the spread of conduct within and among organizations. While we discuss both questions that have received extensive attention, as well as those that have largely escaped notice, we are interested in promoting promising future directions, and hence give the latter more attention. We also position our discussion to be complementary with past work. Our review is preceded by a collection of cases and theory (Punch, 1996), a review of organizational failures and misconduct (Vaughan, 1999), and a review of unethical behaviors at the individual level (Tenbrunsel & Smith-Crowe, 2008). We build on these and extend them with more recent theoretical and empirical work, with a special emphasis on research that received less attention in these treatments. In some places where the evidence on misconduct is thin, we mention evidence on other outcomes that are relevant to the theories we discuss. We emphasize misconduct at the organizational level of analysis, and we are especially interested in how organizational structures, processes, and relationships give rise to misconduct.

Our discussion will unfold as follows. First, we provide a rigorous definition of misconduct. We then review the literature on the causes of misconduct, beginning with the individual, then progressing to the rational choice, strain, cultural, network, organizational, and inter-organizational explanations. Next, we develop the role of social-control agents in creating and labeling misconduct. We then explore the consequences of misconduct for organizations, networks, and individuals. We close with a discussion of some of the surprises we encountered in conducting this review, and by proposing fruitful areas for future research.

## Definition of Misconduct

The development of precise concepts is thought by many to be fundamental to the progress of all fields of scientific inquiry (Blumer, 1931). This is particularly true in the case of concepts pertaining to the objects of inquiry, because researchers need to identify clearly what they are studying in order to allow comparison and cumulative work. Unfortunately, those studying misconduct in and of organizations have not heretofore offered precise, or even necessarily consistent, definitions of misconduct. There is good reason for this failure to arrive at a universally accepted precise definition: organizations are situated in environments that contain many different constituents, and are studied by scholars who embrace different disciplinary perspectives, each of which tends to have somewhat different points of view on the distinction between appropriate and inappropriate conduct.

Tenbrunsel and Smith-Crowe (2008) recommend addressing this problem by turning to the fields of philosophy and theology. This suggestion has merit, insofar as both fields have devoted a substantial amount of rigorous effort to the subject of distinguishing between admirable and reproachable behavior, but it also has a weakness. Even these fields exhibit considerable diversity with respect to the understanding of morality and ethics, however, and thus will not yield a universally agreed conception of misconduct. Instead, we turn to sociology and, more specifically, labeling and conflict theory for guidance (H.S. Becker, 1963; R. Collins, 1975; Coser, 1967; Lemert, 1951; Schur, 1971).

We define organizational misconduct as behavior in or by an organization that a social-control agent judges to transgress a line separating right from wrong; where such a line can separate legal, ethical, and socially responsible behavior from their antitheses. We define a social-control agent, in turn, as an actor that represents a collectivity and that can impose sanctions on that collectivity's behalf. Judgment by a social-control agent is the crucial link in this definition, because it allows for examination of when a line separating right from wrong is invoked and how transgression of such a line is judged to have occurred. The indefinite singular "a social-control agent" also matters because organizations may be judged by multiple agents, and a definition that allows any of these to make the judgment opens for investigation of the degree of agreement among social-control agents on misconduct judgment. Our definition avoids treating misconduct as a straightforward implication of a set of laws, ethical principles, and/or social norms. Such standards are obviously involved in judging behavior to be misconduct, but they may be applied selectively or inconsistently. Although our definition has the drawback of needing to distinguish between social-control agents and other concerned actors, a distinction that is likely to be subject to dispute, it also has two important benefits.

First, defining misconduct in this way makes the identification of misconduct an empirical question; that is, it becomes a question of using empirical evidence to determine the extent to which a behavior is designated as an instance of wrongdoing by social-control agents. Second, defining misconduct in this way allows researchers to take into account and analyze an observable environmental variable of importance to managers. It is an indisputable fact that the position of the line between right and wrong is variable; consequently, managers can move from the right to the wrong side of the line without changing the way they behave. Further, it is an indisputable fact that the movement of the line between right and wrong over time and across places presents a practical problem of some consequence to managers, insofar as organizations and managers on the wrong side of the line frequently incur serious penalties. Indeed, theoretical work has identified social-control agents as critical to determining which managers will bear personal blame for organizational failures, and which will avoid blame (e.g., Wiesenfeld, Wurthmann, & Hambrick, 2008). Rigorous use of a social-control-agent definition of misconduct, paired with empirical research on the behavior and influence of social-control agents, would be a major contribution to research on organizational misconduct.

The designation of social-control agents is made so as to allow the development of theory that improves our understanding of the phenomenon in question: misconduct in and by organizations. We consider the world polity (i.e., international governing bodies), the state (i.e., national and local governmental bodies), and professional associations (e.g., the American Medical Association, the American Bar Associations) as social-control agents. Each of these entities represents a larger collectivity, and has the capacity to impose significant sanctions on its behalf. We omit more general audiences such as customers, or specific-interest groups without an official standing such as non-governmental organizations or lobby groups. While these actors react to misconduct and sometimes seek to redefine it (Hoffman, 1999), we think that their role is better treated in theories of politics and social movements (e.g., McCarthy & Zald, 1977). We view the mainstream media as an intermediate category, as the media can impose public scrutiny and humiliation, which is a form of sanction; although it cannot impose punitive sanctions of the form that the state or professional bodies control, the media has the ability to frame behaviors as misconduct and put pressure on social-control agents to put such sanctions in place. Later, we discuss how social-control agents draw the line between right and wrong and the role of the media.



### Level of Analysis

We examine misconduct at the organizational level of analysis. We are especially interested in how organizational structures, processes, and relationships give rise to misconduct in and of organizations. We are also interested in how organizational factors influence the likelihood that behavior in and of organizations becomes defined as misconduct, and how the labeling of behavior as misconduct influences the fates of organizations. With this said, it is extremely difficult and perhaps inadvisable to elaborate an organization-level analysis of misconduct without taking into account individual-level processes and outcomes. The characterization of organizations as actors is, after all, a legal fiction. Many organization-level analyses are predicated on assumptions about individual behavior. Thus we must at least briefly consider theories about misconduct that operate at the individual level of analysis. Further, much organizational misconduct begins with the actions of one or a small number of individuals, so we must consider how misconduct that emanates from the behavior of individuals or groups becomes an organizational phenomenon. Finally, the labeling of misconduct can impact the fates of organizational participants, especially leaders. We consider the first of these three topics here, and the second and third in subsequent sections.

Individual-level theories of misconduct, as they pertain to organizational-level misconduct, fall into two broad categories. The first assumes that individuals decide based on normative assessments about the appropriateness of a course of action (March, 1994). When they conclude that a wrongful course of action is consistent with the norms, values, and beliefs they hold, they essentially conclude that the wrongful course of action is, in fact, rightful, and thus they proceed with the course of action. The second assumes that individuals engage in consequential decision making by examining the pros and cons of a wrongful course of action, and chose wrongful courses of actions when they conclude the pros outweigh the cons (March, 1994). This approach is extremely flexible, allowing for normative considerations to be included in cost–benefit calculations (e.g., the guilt associated with violating a norm might constitute a con of a wrongful course of action).

There is a large volume of research on individual variation in the pursuit of wrongful courses of action, much of which examines the correlation between variables presumed to be related to individuals' preference structure (e.g., their age) or their norms, values, and beliefs (e.g., professional training). The most theoretically advanced research at the individual level examines the decision processes people invoke when making ethical decisions (see Tenbrunsel & Smith-Crowe, 2008, for a comprehensive review of this literature). Rest (1986) provided the foundation for early theory in this tradition, introducing a model that assumes that people progress through four stages when making ethical decisions: awareness that a decision has ethical implications, judgment regarding an ethical course of action, formation of an intention to act, and action. An important assumption of this model is that rationality guides a person's progression through these four steps. Research in this tradition focuses on identifying the individual (e.g., gender) and contextual factors (e.g., organizational climate) that influence individuals' progression through the four states that produce ethical awareness, judgment, intent, and behavior.

Recently, ethical-decision theorists have begun to call this model into question in two important respects. First, some have questioned the extent to which organizational participants deliberate in a rational fashion when confronted with ethical decisions. These decision theorists examine how bounded rationality can lead organizational participants to fail to recognize the moral nature of situations (Butterfield, Trevino, & Weaver, 2000; Jones, 1991; Reynolds, 2006). They also examine how bounded rationality can cause organizational participants to formulate judgments, intentions, and actions that are unethical, even though these judgments, intentions, and actions contradict their closely held values and beliefs. A raft of studies now shows that cognitive constraints prompt individuals to predict that they will behave more ethically than they do and to believe that they have behaved more ethically than they have (Tenbrunsel, Diekmann, Wade-Benzoni, & Bazerman, forthcoming). Moreover, cognitive limitations prevent them from comprehending and correcting their own biases (Messick & Bazerman, 1996; Moore, Tetlock, Tanlu, & Bazerman, 2006) and from maintaining their moral standards (Bandura, 1986, 1999). Second, some have begun to question the extent to which organizational participants deliberate at all when confronted with ethical decisions (Damasio, 1994; Green & Haidt, 2002; Haidt, 2001). These researchers focus on the role that unconscious motivations, intuition, and emotion play in ethical decision making.

Perhaps the most comprehensive of the new ethical-decision-making theories is moral seduction theory (Moore et al., 2006). It holds that most individuals are unaware of the pressures they face because of several common decision-making biases. First, individuals are subject to selective perception, such that they evaluate data differently when they have a stake in a given decision, and focus attention on evidence that leads them to their desired conclusion (Lord, Ross, & Lepper, 1979; Russo, Medvec, & Meloy, 1996, 1998). Second, they fall prey to the bias of plausible deniability, or the willingness to endorse the biased proposal of another actor (Diekmann et al., 1997); this makes it easier for the focal actor to proceed on the basis of existing decisions, although they may seem suspect. Escalation of commitment to a previous course of action (Brockner & Rubin, 1985; Staw, 1976) then leads actors to justify questionable decisions rather than to reassess actions that may lead to misconduct. Forcing actors to justify and become accountable for their judgments may lead to further commitment to previous decisions, as well as additional justification (Staw, 1976; Tetlock & Lerner, 1999). Finally, the fundamental attribution error leads individuals to attribute their own actions to situational factors, while assigning personal responsibility to the actions of others (Jones, 1979). This effect is exacerbated by narrow roles that disperse responsibility (Ermann & Lundman, 2001).

Our investigation of organizational misconduct at the organizational level of analysis will, to varying extents, build on these individual-level theories and research. For example, rational-choice theory assumes that organizational participants are cost–benefit calculators, whereas culture theory assumes that organizational participants are normative appropriateness assessors. Similarly, accident theory assumes that organizational participants are boundedly rational actors, and the collective corruption literature builds on moral seduction theory. It is to these organization-level theories of misconduct, and others, to which we now turn.

## The Causes of Misconduct

Many organization-level theories have been offered to explain the genesis of misconduct in and by organizations. We review what we believe to be the five main organization-level theories, which emphasize the role played by rational choice, strain, culture, networks, and accidents. Although our review highlights the conceptual differences between these theories, we readily acknowledge that (and in a few places explicitly suggest how) these theories may be considered complementary, and thus can be used in consort to explain specific instances of organizational misconduct.

*Misconduct as a Rational Choice*

Rational-choice perspectives focus on individual or organizational actors. In economics, agency, contract, and reputation theories address the issue of social control of individually rational actors (Grossman & Hart, 1983; Kreps & Wilson, 1982; Milgrom & Roberts, 1988; Shapiro, 1982). These theories are associated with a recent trend toward taking economics beyond markets and into the internal workings of firms (e.g., Lazear, 2000), but they are revisiting older issues. This research started with the claim that managers had distinct interests and an ability to control the firm that led corporations to different goals than those intended by their owners (Berle & Means, 1932). The "managerialist thesis" contained a general view of organizations as arenas with contested goals, as well as specific suggestions on how managerial goals of stable growth rates led to foregone profits, an idea that is connected to research on goal displacement (Selznick, 1949) and dominant coalitions (Cyert & March, 1963) in organizational theory. Lately, the focus on growth goals has been replaced by an interest in a broader range of managerial behaviors such as inappropriate risk taking, manipulation of accounts, or outright fraud, bringing this theory into the realm of misconduct research.

Rational-action modeling assumes self-interested actors who need to be controlled in order not to choose actions that would be beneficial for them but harmful for transaction partners or third parties (Arrow, 1963). The modeling often implies that some level of misconduct will occur because optimal control mechanisms make a trade-off between control costs and misconduct costs, which is usually not reached by eliminating misconduct. Thus these models can involve "rational misconduct," actions that are chosen because their benefits exceeds the expected sanctions for the individual, and "optimal misconduct," actions that occur at a level where the marginal costs of added control exceed the marginal benefits to society (G.S. Becker, 1968). In other words, from the perspective of rational-choice theory, a certain level of misconduct is normal and expected within any social system. The models help identify the conditions under which transactions cannot be governed by the exchange partners only, and hence there is justification for a social-control agent to detect and sanction misconduct.

*Misconduct against organizations.* Principal-agent models assume that one actor (the agent) generates observable outcomes for another (the principal), but the outcomes are influenced by a combination of environmental influences and the agent's unobservable actions (Grossman & Hart, 1983; Holmstrom, 1979). This creates the moral-hazard dilemma: the agent is not willing to make full effort when the principal cannot distinguish effort from luck, and thus is unable to fully reward the effort. Although the basic principal-agent model assumes a hierarchy where the principal pays for work and obtains profits, it generates insights that are useful in contexts such as insurance fraud by consumers and fraud and deception by providers of financial products. A key insight is that paying for performance is inferior to payments that also rely on other signals (Dutta & Radner, 1994; Holmstrom, 1979), which is the rationale behind recommendations for governance mechanisms that involve some form of direct monitoring, as in the burgeoning literature on boards of directors (Dalton, Hitt, Certo, & Dalton, 2007; Hillman & Dalziel, 2003; Peasnell, Pope, & Young, 2005; Westphal, 1998). A common form of managerial misconduct caused by paying for performance is misreporting of earnings, as in the large literature on upward earnings management and earnings smoothing (e.g., Bergstresser & Philippon, 2006; Harris & Bromiley, 2007; Zhang, Bartol, Smith, Pfarrer, & Khanin, 2008); misreporting of earnings is illegal, but difficult to detect. These managerial reactions to incentive pay are essentially identical to how laborers react to Taylor-style piece-rate compensation systems.



Principal-agent models can be used to explain misconduct by an employee against the organization, or a manager against the owners of the organization. The ease of deriving predictions on potential misconduct from these models has caused them to be widely applied in the form of "popular" agency theory, which promotes a set of practices that are thought to reduce managerial pursuit of own interests at the expense of owners. For example, the literature on executive compensation compares top executive compensation packages with agency-theory principles of linking pay to performance (Murphy, 1999). This is a voluminous literature, but its link to agency-theory predictions are weakened by the difficulty of specifying how the performance and pay should be related, because different agency models specify different relations (Murphy, 1999). Similarly, there is a large literature testing the proposition that an independent board of directors control managers better (Fama, 1980; Fama & Jensen, 1983), although recent evidence that independent boards of directors are more likely to abandon companies after revelations of misconduct (Pozner, 2007) calls into question their desire to control managers. Although both theories offer insights into how managers can be made less likely to defraud investors and customers, strictly speaking these are general behavioral predictions along the lines of "probability of detection is inversely related to crime."

Formal principal-agent models yield specific predictions on how popular agency-theory practices are likely to fail. These predictions stem from the observation that many principal-agent models have an unrealistically narrow range of actions available to the agent (Holmstrom, 1992). For example, stock options make agents choose actions that owners would choose, provided the available actions are restricted to effort and investment choices. Principal-agent models where the agent can divide effort between influencing their actual performance and a signal that influences outsiders' estimate of their performance, however, show that the agent will rationally spend effort influencing the signal (Milgrom & Roberts, 1988). Empirical work has shown that managers with a high level of potential stock-option compensation are more likely to manipulate accounts in order to influence their firm's stock value (e.g., Harris & Bromiley, 2007; Zhang et al., 2008), consistent with the influence prediction. An important restriction of these models is the need to specify the actions that the agent can take in some detail, but managers bent on self-enrichment can be very creative, leading to cases of misconduct that would have been difficult to predict. For example, it was thought that managers would either smooth earnings or overstate earnings, but recent research has shown that many firms miss earnings announcements just before option grants, thus creating a dip in the stock value that lowers the exercise price of the options (McAnally, Srivastava, & Weaver, 2008). Alternatively, they may just postdate the option to a day when there was a dip in the firm's stock value (Lie, 2005). Although boards of directors are obliged to prevent such managerial extraction of stockholder value, there is evidence that they too benefited from option backdating and contributed to its spread among firms (Bizjak, Lemmon, & Whitby, 2009). Thus the theoretical predictions on conditions that lead to specific forms of misconduct do not imply that all misconduct can be eliminated by removing those conditions.

*Misconduct by organizations.* Agency theory is focused on misconduct by actors lower in a hierarchy (agents) against actors higher up (principals), and thus does not address misconduct against peers. Organizational misconduct relative to a transaction partner is instead treated in contract theory, which looks at the problem of providing goods and services with some unobservable characteristics, as when there is variation in product quality and safety that cannot be assessed immediately by the customer (Akerlof, 1970). Unobservable product quality leads to a broad range of misconduct at various levels of illegality and enforceability, with the car salesperson and the financial advisor being frequent examples of organizational actors who have an informational advantage over their transaction partners. The literature provides easy solutions to this problem in two special cases. First, in the case of repeat purchase, the buyer can discipline the seller through the threat of finding another transaction partner (Shapiro & Stiglitz, 1984). The main prediction is that the threat of terminating the exchange relation and delay in finding a new exchange partner ("unemployment") is sufficient to deter the seller from deception. Second, the seller can issue a warrantee against problems that existed at the time of purchase but surface later, or the buyer can promise a bonus if a certain level of performance is achieved (Akerlof, 1970). These devices are identical if both the buyer and the seller can commit to the promised warrantee or bonus, and, in practice, seller warrantees are common because the seller tends to be a long-lived player (such as a firm) with a reputation at stake, while the buyer can be a one-shot player such as an individual buying a car. Again, the finding is that deception can be deterred.

In markets with these characteristics, some economists would argue that there is little need to create a set of rules and a strong social-control agent, as they are self-regulating, such that misconduct is ultimately found out and dealt with appropriately. Many goods are purchased so infrequently, however, that the threat of ending repeat purchases kicks in too slowly, and there is a difference between extending a warranty and honoring it. Ford's response to the flaws of the Pinto design is a good illustration of organizations being reluctant to admit faults that would trigger warrantees or other financial restitution (Punch, 1996). Likewise, when B. F. Goodrich supplied defective brakes to the A7D attack aircraft development project, it may have relied on the negotiated nature of defense procurement to save the day (when the defects in the brakes were discovered, Goodrich was indeed given the task of developing a new brake that could perform up to specifications). Failures of self-regulation are frequent enough that there is clear recognition in the rational-choice literature that these models are limited.

To overcome the limitations, rational-choice theorists have developed two types of reputation models. In one, the reputation is seen as a capital stock that adds to the value of the product offered by a firm but can be depreciated by failing to perform to the required standards (Klein & Leffler, 1981). These models are most easily motivated in the case of quality reputations, but can also be extended into spillovers from other types of events, such as financial misconduct, to customer reactions against the firm in the form of lower demand. In the other, reputation influences how other actors will react to the firm when they encounter it in a repeated game (Kreps & Wilson, 1982). The capital model can be justified as a solution to a repeated game, so basic versions of these models are compatible with each other. Repeated game models better handle situations in which the reputation concerns discrete types of firms (e.g., honest or deceptive) instead of grades along a range (e.g., quality), and are easier to generalize to contexts where information flows about the misconduct are restricted. Reputation models have been applied in research on defense-contracting fraud, which is a rich empirical context because of its frequency: one study found 249 cases of (alleged) fraud between 1983 and 1995 (Karpoff, Lee, & Vendrzyk, 1999).

Reputation models generally predict rigid behaviors on the part of firms because they assume penalties for a downward deviation such as misconduct, and an absence of rewards from upward deviations such as higher than expected quality. They also specify when misconduct is likely: low-reputation firms are more likely to commit misconduct because they have less to lose, and firms that experience adverse conditions such as unexpected increases in costs are more likely to commit misconduct because they now have a mismatch between the cost structure and the optimal behavior (Lott, 1996). If adverse conditions can be detected through profitability, the theory predicts a higher incidence of misconduct in low-performing firms, similar to the prediction made by strain theory, which is described next. This prediction is well known from both the law- and management-studies approaches to organizational misconduct, and can also be derived from a behavioral-theory perspective (Clinard, Yeager, Brissette, Petrashek, & Harries, 1979; Staw & Szwajkowski, 1975). It is important, however, to distinguish firm-specific performance from environmental up- and downturns, as rational-choice models also predict that firms are more willing to risk sanctions during upturns because of the greater rewards that can be gained when demand is high.

The prediction from reputation theory that has been subjected to the most scrutiny is the link between firm performance and misconduct, but this prediction overlaps with that of strain theory, discussed next, and thus is not unique to reputation theory. There has been remarkably little work on the prediction that high-reputation firms are less likely to commit misconduct, although some supportive evidence from electronic marketplaces exists (Gregg & Scott, 2006). Given the key role of this prediction for the theory, it ought to be an important topic for future research.

### *Strain as a Source of Misconduct*

Strain theory is a sociological extension of rational-choice theory. Strain theory holds that actors resort to misconduct when they are unable to achieve their goals through legitimate means. Although Merton (1938) formulated strain theory to explain why the lower classes of society were more likely to engage in illegal activity, there is considerable evidence that strain caused by the gap between goals and actual achievement leads to misconduct at all levels of society (Agnew, Piquero, & Cullen, 2009; Clinard & Yeager, 1980; Vaughan, 1999). Moreover, the achievement gaps that drive individual misconduct—the inability to meet desired goals, the actual or potential loss of valued outcomes, and the actual or potential acceptance of negatively valenced outcomes (Agnew et al., 2009)—may also drive organizational misconduct when individuals engage in misconduct in and on behalf of organizations. For example, Zhang et al. (2008) found that organizations are more likely to manipulate earnings when CEO stock options are out-of-the-money, introducing a gap between the actual and potential earnings of the CEO.

Misconduct may arise from strain stemming from organization-level goals, rather than individual-level ones. Simpson (2002, p. 8) writes that organizational misconduct may "have little to do with an individual employee's needs but a lot to do with organizational contingencies, priorities and needs." That is, when the organization is under strain, individuals who internalize the achievement gap may be motivated to engage in misconduct. Thus research shows that failing and marginal organizations (Agnew et al., 2009; Vaughan, 1999), as well as those confronting resource scarcities (Finney & Lesieur, 1982; Vaughan, 1983), are the most likely offenders. Studies also show that misconduct is related to financial problems at the organizational level (e.g., Clinard &

Yeager, 1980; Simpson, 2002; Staw & Szwajkowski, 1975), although restrictions of internal information distribution and incentives to check are also implicated (Schnatterly, 2003). In general, studies find that misconduct is more prevalent in for-profit companies (where performance pressures are assumed to be high), firms with relatively low or declining profits, firms in depressed industries, and firms suffering from other problems such as threats to the competitive position (Vaughan, 1999; Wheeler, 1992). One study reports the apparently contradictory finding that prominent organizations become more likely to engage in misconduct after having higher performance than their peers, although the authors suggest that this reflects managerial attempts to meet accelerating expectations for performance (Mishina, Dykes, Block, & Pollock, forthcoming).

Finally, misconduct can result from the strain associated with power and status contests. Loss of existing status and inability to achieve status goals (Wheeler, 1992), declines in social positioning or standing (Wilmot & Hocker, 2001), and retaliation for perceived injustice (Andreoli & Lefkowitz, 2009; Griffin & O'Leary-Kelly, 2004) may also promote organizational misconduct. According to Vaughan (1999), contests of power often result in organizational misconduct among powerful organizations, as well as cooptation of the regulatory process designed to discourage such behavior (Michalowski & Kramer, 1987; Snider & Pearce, 1995). This might explain why some studies find that high-growth firms are more likely to engage in misconduct than their less successful peers (e.g., Clinard & Yeager, 1980), and that moderate to very good performance is more closely associated with misconduct than poor performance (e.g., Baucus & Near, 1991; MacLean, 2008). Because competition is endemic, all organizations are vulnerable, regardless of organizational condition; the weak are tempted to engage in misconduct to gain position, the strong are tempted to maintain position.

Clearly, research in the strain tradition has produced a number of valuable findings, but these findings are sometimes difficult to square with one another. Although theorists have offered sensible ways to accommodate individual sets of apparently contradictory findings, it remains the fact that some studies show that weak and declining performance lead to misconduct, while others show that strong and improving performance lead to misconduct. We think that a better integration of the conflicting results might be achieved by considering the role of managerial aspiration levels (Cyert & March, 1963; Greve, 2003; Harris & Bromiley, 2007). Managerial aspiration levels for organizational performance are set by comparison with the performance of peer organizations and with the past performance of the same organization. Thus strain might occur in a firm experiencing high performance if that performance is low relative to its past performance, whereas strain might occur in a firm experiencing increasing performance if that performance is low relative to its peers' performance. By modeling how aspiration levels are set, researchers might be able to arrive at a more consistent set of findings on organizational performance and misconduct (Harris & Bromiley, 2007).

*Culture as a Cause of Misconduct*

*How culture facilitates misconduct.* Cultural theories of misconduct have been posed at multiple levels of analysis, including occupations, professions, organizations, industries, societal sectors, and societies. We focus primarily on organization-level theories. Regardless of level, culture can be said to consist of assumptions about the nature of the world (e.g., the extent to which human nature is fundamentally competitive as opposed to cooperative), as well as norms, values, and beliefs about the kinds of attitudes and behaviors that are appropriate and good (e.g., the degree of truthfulness that employees should exhibit). Organizational cultures are conveyed through a variety of forms, such as language, rewards and punishments, and leader behavior (Ashkanasy, Windsor, & Trevino, 2006; Hegarty & Sims, 1978).

While organizational cultures may condemn certain types of misconduct, they provide support for others (Coleman & Ramos, 1998; MacLean, 2008). Organizational cultures can provide normative support for misconduct in three main ways. First, they can endorse misconduct (e.g., Bensman & Gerver, 1963: Punch, 1985; Shulman, 1997) with varying degrees of explicitness (Ashkanasy et al., 2006). Least explicitly, a culture can focus members of a community on achieving ends without simultaneously providing guidance about the means with which ends should be achieved; some contend that organizational cultures in capitalist economies exhibit this character (Finney & Lesieur, 1982). More explicitly, a culture can focus members of a community on achieving ends while simultaneously conveying—sometimes subtly—a lack of concern about the moral character of the means with which ends should be achieved. For example, Kulik (2005) contends that Enron's culture was characterized by agency-theory reasoning, which placed paramount importance on personal and corporate economic gain and little importance on adherence to rules of any kind. Even more explicitly, a culture can convey acceptance and appreciation of actions that break rules and violate norms, particularly those that value risk taking (Vaughan, 1999) or innovativeness. Sims and Brinkmann (2003) contend that Enron's culture also placed a high value on cleverness, which implicitly encouraged rule-breaking. Occasionally, cultures can even endorse specific kinds of misconduct; at Archer Daniels Midland, for example, employees were familiar with the motto, "the customer is our enemy, our competitors are our friends." The assumption telegraphed by this motto, that ADM employees should look more kindly on their competitors than their customers, might have provided an ideational foundation for employees' efforts to establish price-fixing agreements with their competitors in the lysine market, for which they were ultimately successfully prosecuted and fined (Eichenwald, 2000).

Second, organizational cultures can permit misconduct under certain extenuating circumstances. Sykes and Matza (1957) first drew attention to cultural content of this sort, which they labeled "techniques of neutralization," in their study of youth gangs. Ashforth and Anand (2003) recently applied Sykes and Matza's insights to organizational wrongdoers, identifying a variety of techniques of neutralization that assuage the guilt that organizational participants might otherwise feel when engaging in misconduct, including: denial of victim, denial of injury, denial of responsibility, social weighting, appeal to a higher authority, and balancing the ledger. For example, the denial-of-victim technique conveys the message that it is acceptable to harm others when those who are harmed deserve to be harmed (i.e., are not really victims). For instance, the culture of Salomon Brothers, as described by Michael Lewis (1990), assumed that their clients were stupid and that stupid people deserved to be exploited. This cultural content could be used to justify counseling clients to purchase investments that earned the firm superior commissions but earned its clients inferior returns.

Third, organizational cultures can give rise to other conditions that, in turn, facilitate misconduct. This is most obviously the case when cultures place a high value on achieving extraordinary performance. For example, Enron employed a forced ranking system when evaluating employees, leading employees to feel substantial pressure to outperform their peers (Sims & Brinkmann, 2003). This might have generated the type of strain, described above, that could lead employees to adopt illegitimate means of achieving legitimate goals.

*Where culture comes from.* Leaders are thought to play a crucial role in developing and disseminating organizational culture (Schein, 1985). Surveys indicate that leadership behavior is the factor that most strongly influences individuals' willingness to engage in misconduct (Baumhart, 1961; Brenner & Molander, 1977). Even if not explicitly engaging in corruption, by allowing, rewarding, or ignoring it, leaders may authorize misconduct, be it implicitly or explicitly (e.g,, Ashforth & Anand, 2003; Brief, Buttram, & Dukerich, 2001; Kelman, 1973). Building on Schein's (1985) analysis of how leaders disseminate cultural content, Sims and Brinkmann (2003) examine five dimensions of leader behavior that can facilitate the dissemination of cultures of misconduct: the things to which leaders pay attention, the ways in which they respond to crises, the behaviors they model, the behaviors they reward and punish, and the kinds of employees they hire and dismiss. This perspective implies a relatively optimistic view of how to combat culture-facilitated organizational misconduct. Installing top managers who attend to the proper things, respond to crises in the proper way, model the proper behaviors, reward and punish employees for proper behaviors, and hire and dismiss the right employees can transform a wrongful culture into a rightful one.

Cultural content can also emerge in a less agentic fashion, however. Even scholars who believe leaders play a crucial role in developing and disseminating cultures acknowledge that cultures help organizations solve fundamental problems of external adaptation and internal integration (Schein, 1983). This view is rooted in the structural functionalist analysis of culture (Radcliffe-Brown, 1965), and is consistent with the organizational ecology approach, which contends that organizations with cultures that are well adapted to fit their environment can have a survival advantage over organizations with cultures that are less well adapted (Carroll & Harrison, 1998). These perspectives imply a less optimistic view of how to combat organizational misconduct, because they suggest that organizational cultures will tend to reflect their environment, regardless of how committed leaders are to pushing them in a different direction.

*Misconduct in Networks*

Network theories of organizational misconduct occupy an intermediate position between individual-level theories and the organizational-level theories discussed below. Individual-level theories of misconduct tend to assume that organizational participants embark on wrongdoing as independent actors. When these theories take the social context into account, they conceptualize it in relatively undifferentiated terms (e.g., as "climate"). Rational choice, strain, and culture accounts explicitly theorize the social context, but they do not analyze how individuals differ in their behavior within this context. For example, a culture of misconduct may provide a good explanation of the average propensity of organizational participants to commit misconduct, but it cannot explain variation in participation across organizational participants; this is where network theory comes in.

Many cases of misconduct involve multiple individuals linked by social ties. Indeed, many cases of organizational misconduct are collective efforts intentionally orchestrated by a number of interconnected individuals. For example, the falsification of test reports in the B. F. Goodrich brake scandal involved multiple managers overseeing and instructing the engineers in charge of conducting and reporting the tests (Punch, 1996). There are even cases of coordination among firms involved in joint misconduct, as in the price fixing in the heavy-electrical-equipment industry, where three of the networks involved between 21 and 33 individuals spread across many companies (Baker & Faulkner, 1993). Such patterns of participation suggest that social networks structure organizational misconduct (Brass, Butterfield, & Skaggs, 1998). Theoretical accounts for the network effect on misconduct come in two variants, which can be labeled the influence account and the secrecy account respectively.

The influence account treats network effects on misconduct in much the same way as it treats network effects on other forms of behavior. Social networks facilitate observation and communication among actors, and tend to align opinions, although the effect is weaker for controversial issues (Erickson, 1988; Huckfeldt, Johnson, & Sprague, 2004). The alignment of opinion among closely connected individuals is an important precondition for misconduct because it can result in local nonconformity to broader norms of conduct. Thus agreement with the norms that social-control agents seek to impose is uneven, and deviations are likely to be particularly strong in parts of the network that are densely connected internally but relatively isolated from the rest of the network, as such isolated cliques are especially capable of developing distinct norms and behaviors (Brass et al., 1998).

While the influence account appears initially to predict opinions rather than behaviors, the predictions carry forward to behaviors as well. It is well known that network ties predict imitation (Rogers, 1995), but a specific finding of greater interest is the contingent effects of networks when a practice is controversial. In such cases, localized clusters of individuals are more likely to adopt the controversial practice (Davis & Greve, 1997), while connections to the broader network instead leads to adoption of less controversial practices (Briscoe & Safford, 2008). Substituting misconduct for controversial practices, the implication is that internally well-connected and globally isolated parts of the network are likely to engage in misconduct.

Contrary to the influence account, the secrecy account treats network effects on misconduct as an intended consequence of the need for secrecy. Social networks can be designed to exclude others from observation of the actions and communications of a set of coconspirators, and work on the organization of illicit activities shows that they take place in networks that fit the theoretical requirements for concealment (Selznick, 1952; Simmel, 1950). Indeed, when misconduct involved inter-organizational coordination, as in price-fixing conspiracies, the network structure that evolved was more consistent with the need for concealment than with the need for coordination (Baker & Faulkner, 1993). The secrecy account assumes a much greater intentionality than the influence account because it is a theory of individuals setting up the structural conditions for committing misconduct undetected.

No studies have yet empirically evaluated the differential validity of the influence and secrecy accounts of organizational misconduct. Hence, the design of studies that might achieve this objective can be considered a priority. But the influence and secrecy accounts of organizational misconduct are not necessarily competing explanations. One can imagine misconduct starting as a result of social influence through a network, and the network subsequently changing during the period of misconduct in order to avoid detection. The key difference in prediction is thus not how networks are associated with the initiation of misconduct, but rather how the network changes once misconduct has started. There is thus also a need for work that examines the evolution of networks involved in misconduct.

*Organizational Accidents and Misconduct*

While the explanations discussed so far have emphasized deliberate misconduct, researchers have also drawn a link between accidents and misconduct. March and Simon (1958) long ago characterized organizational participants as boundedly rational, and organizational task environments as complex, and bounded rationality in the context of complexity can lead to accidents. As Vaughan (1999) describes, accidents may occur either when organizational participants intend to carry out one behavior but unintentionally perpetrate another, or when organizational participants who intend to carry out one behavior planning to produce one set of consequences successfully perpetrate that behavior but produce unintended consequences. Social-control agents can label accidental behaviors, as well as intended behaviors that produce unintended consequences, as wrongful. When this occurs, the organizational participants who perpetrated the behaviors and generate the consequences can be thought to have engaged in accidental misconduct.

The Exxon Valdez oil spill provides a good illustration of the first type of accidental misconduct. The ship's captain and first mate intended to steer the Valdez through the main channel of the Prince William Sound and deliver its cargo safely to its destination, but instead ran the ship aground and spilled its cargo of oil, causing extensive damage to the local fishery and the larger environment. The act and its consequences were considered wrongful by a number of constituencies, resulting in a criminal prosecution and several civil suits (Lev, 1990). Bear Stearns's association with a fraudulent stock-brokerage firm appears to provide a good example of the second type of misconduct. Bear Stearns performed exemplary service as A. R. Baron and Company's clearing agent, but in doing so it unintentionally (or so it claimed) aided and abetted Baron's pursuit of illegal boiler-room practices. Bear Stearns's involvement with Baron and the damage it caused was considered wrongful by the SEC and the brokerage firm's injured clients (Cohen, 2009, p. 239).

*The causes of accidental misconduct.* The bounded rationality of organizational participants and the complexity of their task environments combine to make accidents and, by extension, accidental misconduct endemic to organizational life. Even the most capable organizational participants in the simplest task environments can be expected to make mistakes. Research has identified technological systems, organizational structures, and the normalization of deviance as factors that increase the likelihood of accidents, and thus accidental misconduct, in organizations.

Technological systems are sometimes designed in ways that fail to take into account important known natural scientific principles and facts, which may lead systems to fail in ways that can violate laws and/or cause harm, both of which can cause organizational behavior to be labeled wrongful. This appears to have been the case in the 1963 Vaiont Dam failure near Venice, Italy. Engineers who designed the dam did not take into sufficient account the fact that once the Dam's reservoir was filled, its walls would be subjected to forces that would cause them to collapse, suddenly filling the reservoir with a large volume of dirt and simultaneously displacing a large volume of water, leading to the dam wall overspilling. When this in fact occurred, the valley below the dam flooded, 2000 people were killed, and several of the dam's designers were prosecuted and convicted (Paolini & Vacis, 2000).

Even otherwise well-designed technologies are susceptible to failure. Charles Perrow (1984) has developed a theory that identifies the types of technologies that can give rise to such failures, which he calls "normal accidents." Perrow contends that technological systems that are composed of complex and tightly coupled interactions are prone to fail. Complex interactions are unexpected, either because they are not designed into the system or because they are designed into the system but occur infrequently. Complex interactions are also hard to comprehend, either because they are not well researched or because they are difficult to observe. Tightly coupled interactions are rapid and unmediated relationships; relationships that unfold quickly and unconditionally. Complex, tightly coupled interactions are hard to manage because system operators cannot anticipate them and do not have the knowledge, time, and/or the means to respond to them when they arise.

Perrow (1984) developed his theory to explain accidents in industrial and related systems, such as petrochemical refineries, nuclear power plants, commercial airliners, and seagoing ships. Mezias (1994) extended normal accident theory to explain failure in a financial system, arguing that the savings and loan crisis of the early 1990s was the result of increasing complexity and tight coupling in the industry. Over the decades leading up to the crisis, financial markets became global, trading became continuous (round the clock), new technologies were instituted, the pace of transactions accelerated, new sophisticated financial instruments were created, and a bewildering array of government regulations were promulgated, all of which increased the number of unexpected and unmanageable interactions. Palmer and Maher (forthcoming) offer a similar analysis of the recent mortgage meltdown.

Perrow (1984) and Mezias (1994) consider normal accidents and misconduct to be mutually exclusive because they consider misconduct, by definition, to be intentional and accidents, by definition, to be unintentional. Thus Perrow developed a special label, "executive failure," to denote events that appear to be normal accidents but are in fact incidents of misconduct. Similarly, Mezias contrasted his normal-accident explanation of the S&L crisis with a misconduct account, contending that the evidence fitted the normal-accident explanation better than the misconduct one. Nevertheless, because we define misconduct in a way that is independent of perpetrators' intentions, as behavior that is labeled wrongful by social-control agents, we consider complexity and tight coupling as possible causes of misconduct.

The 1984 Union Carbide accident in Bhopal, India, provides a good example of how complexity and tight coupling can facilitate accidental misconduct (Shrivastava, 1991). When water unexpectedly entered a tank containing methyl isocyanate (MCI) at the Bhopal plant, the two substances reacted to produce toxic MIC vapor and generate high temperatures and pressures, which led to the release of the vapor, all before the operators could diagnose and correct the situation. Sadly, the spread of the MIC vapor into the surrounding community led to over 3000 deaths and many more serious injuries. There is evidence that the plant's operators, superiors, and even its owners did things, discussed below, to increase the likelihood that the plant would fail in this way, but we think that these things contributed to, rather than nullified, the role that complexity and tight coupling played in the accident.

Organizational structures are sometimes designed in ways that fail to take into account important known social scientific principles and facts. When this is the case, they will be prone to fail in ways that can violate laws and/or cause harm, which can cause organizational behavior to be labeled wrongful. Vaughan (1999) contends that there is now a rather large body of organization theory that specifies the appropriate relationship between organizational environments and organizational structures, as well as the appropriate relationship among the various elements of organizational structure. When organization designers fail to take this knowledge into account, accidents are likely to occur. For example, it is axiomatic that as environments become more complex and dynamic, organizational structures need to become more organic, and that as organizations become more differentiated, organizations must adopt integrative devices. When managers design organizational structures without these imperatives in mind, accidents can be expected.

Boston's Big Dig ceiling collapse appears to provide a good illustration of how a faulty organizational structure can give rise to accidental misconduct (Vennochi, 2007). The Big Dig re-routed Boston's main traffic artery through a tunnel beneath the city's downtown area. Shortly after its completion, a concrete tile dislodged from the tunnel's ceiling and fell on a passing car, killing one of its passengers. Several subcontractors directly involved in the ceiling design and installation were forced to pay fines of millions of dollars for behaviors judged to have led to the ceiling collapse. More importantly, the project's general contractors, Bechtel Corporation and Parsons Brinckerhoff, were forced to pay fines of hundreds of millions for failing to provide adequate oversight of the project's ceiling subcontractors.

Even otherwise well-designed organizational structures are susceptible to failure. Organizational structures are designed to economize on decision making under routine circumstances. The division of labor and associated specialization reduces the number of tasks in which an organizational participant needs to become competent. Rules and routines provide organizational participants with clear instructions on how to perform in routine situations, and schemas provide organizational participants with general guides on how to handle modest departures from routine situations. Organizational structures are often ill-equipped to handle significant exceptions from the routine, however; indeed, the more finely tuned an organizational structure is to handling routine matters, the more susceptible it is to failure when exceptions arise.

The failure of Ford Motor Company to recall the Pinto provides a compelling example of how otherwise well-conceived organizational structures can lead to misconduct that is at least partly accidental (Gioia, 1992). Ford's recall coordinator developed a schema for determining whether a car component was sufficiently defective to merit a recall. The schema focused attention on the extent to which a component's failure caused an accident and on the frequency with which it did so. Although this schema enabled the recall coordinator to successfully adjudicate a mind-boggling plethora of candidates for recall, it caused him to underestimate the judiciousness of recalling the Ford Pinto, whose gas tank was susceptible to igniting when struck from behind at relatively low speeds. The gas tank did not fail and, in doing so, cause accidents; rather, it ignited when struck from behind as the *result* of accidents (generally caused by driver error). Further, rear-impact fires were rare, relative to the number of problems causes by other recall candidates.

The normalization of deviance is a process by which technological and organizational systems become faulty (Vaughan, 1996, 1999). Many, if not most, mistakes represent only small deviations from intended behavior, or produce consequences that are only slightly different from those that are intended, and such small deviations in behavior and consequences generally do not produce substantial negative outcomes. As a result, those who make such mistakes and observe that they do not have serious consequences learn from them in a perverse way; namely, they learn that the mistakes are acceptable. As a result, mistakes are repeated and the procedures that generate them are embedded in organizational routines (both written and unwritten); to use Vaughan's term, they are "normalized." Normalization may lead to the institutionalization of deviance within organizational cultures, such that aphorisms like "if you're not cheating, you're not trying" (Levitt & Dubner, 2005, p. 38) take on a normative flavor. When deviance is normalized, the standards against which future deviations are evaluated are loosened, and with each successive loosening of standards, the system becomes increasingly vulnerable to failure (Starbuck & Milliken, 1988).

The Union Carbide plant in Bhopal, India, also appears to provide a good illustration of how the normalization of deviance can facilitate accidental misconduct (Shrivastava, 1991). The plant placed a number of safety devices off-line—some to allow for repair, and some to save money—which might have prevented the accident or reduced its consequences. Importantly, because the removal from service of each safety device was not promptly followed by negative consequences, with the dismantling of each successive safety device, the plant's operators likely were lulled into believing that the safety devices were not really necessary.

Organizational systems can become faulty in a similar way. Work groups develop routines to handle repeated tasks more efficiently, and these combine with the routines of interdependent work groups to increase organizational efficiency over time (Argote, 1999). Routines involve multiple individuals acting in concert, either sequentially or simultaneously (Nelson & Winter, 1982). They are the result of initial design and social evolution, as it is through modifying routines that work groups find ways to increase efficiency. Modifications to increase efficiency often involve shortcuts that decrease reliability and checking, however, and that work as long as "all is well," but not in unusual circumstances. Hence, incrementally adjusted routines create organizational vulnerability.

MCI's fraudulent bookkeeping in the face of the failure of corporate customers to pay their bills might provide an example of this kind of misconduct (Pavlo & Weinberg, 2005). Because one of MCI's biggest customers, WorldCom, was habitually late in making its payments, the MCI executive responsible for collecting customer bills began sending a subordinate to WorldCom's headquarters on the last day of the payment period to accept the check and immediately fax a copy of it back to MCI headquarters. Then the firm recorded the bill as paid, even though the check had not even been deposited in the firm's bank account. Over time, MCI extended this practice to other customers and routinized the process, to the point that the faxed-check entries were widely referred to as "the-check's-in-the-mail" deposits. The routinization of this unacceptable accounting practice set the standard against which other more egregious accounting manipulations were evaluated.

### *Misconduct as an Organizational and Inter-Organizational Phenomenon*

Most of the theories reviewed above explain how the organizational context can increase the likelihood that individuals or small groups of individuals will choose to engage in misconduct. Sometimes misconduct perpetrated by individuals or small groups remains restricted to those individuals or small groups who initiated it. For example, when top managers backdate their stock options, this misconduct typically does not spread through the organization (partly because typically only a small group of individuals in a firm receive stock options). Other times, however, misconduct spreads to others in an organization. When this occurs, the misconduct comes to characterize the organizational as a whole, as appears to have been the case at Enron (Eichenwald, 2005; McLean & Elkind, 2003). Moreover, sometimes misconduct can spread between organizations. When this occurs, the wrongful behavior comes to characterize larger aggregates, such as industries and fields, as appears to have been the case in the heavy-electrical-equipment price-fixing scam of the 1950s (Baker & Faulkner, 1993). Below, we consider the spread of organizational misconduct in organizations and larger aggregates.

*Spread of misconduct throughout an organization.* Brief et al. (2001) and Ashforth and Anand (2003), taken together, elaborate a process model of collective corruption that explains how misconduct perpetrated by one or a few individuals can become an organizational phenomenon. They propose that individual or group misconduct permeates an organization in four stages: initiation, proliferation, institutionalization, and socialization. In the *initiation stage*, top managers embark on a wrongful course of action. Top manager behavior is, in this model, assumed to be the result of cost–benefit analyses of the sort that rational-choice theory presumes, or normative assessments of the sort that culture theorists assume.

In the *proliferation stage*, top managers explicitly or implicitly direct employees further down the hierarchy to implement the misconduct. As indicated above, top managers can disseminate misconduct by fostering a culture that endorses, permits, or creates conditions conducive to misconduct, and can also use formal authority to direct subordinates to engage in misconduct. Once misconduct has begun to spread to lower levels of the organization, it can proliferate through interaction among employees. Social learning (e.g., Bandura, 1986) allows employees to influence co-workers' behavior through modeling (Brown, Trevino, & Harrison, 2005; Robinson & O'Leary-Kelly, 1998). Further, individual-level psychological processes facilitate employees' descent into misconduct. Employees can rationalize misconduct by employing techniques of neutralization, such as denying responsibility, refocusing attention, manipulating language, and minimizing the undesirable nature of misconduct after the fact (Coleman & Ramos, 1998; Gellerman, 1986; MacLean, 2008). Over time, employees may become committed to the wrongful course of action on which they have embarked (Staw, 1976).

In the *institutionalization stage*, misconduct becomes embedded in organizational memory and solidified in routines and organizational structures (Walsh & Ungson, 1991), such that precedent, routines, and structure legitimize the behavior (Ocasio, 1999; Simon, 1967). Once the practice of misconduct becomes embedded, a culture of misconduct can develop and lead members of the organization to believe that misconduct is acceptable (Ashforth & Anand, 2003). Misconduct becomes understood as "the way things are done," and thus a *de facto* rule of behavior (Brass et al., 1998; J. Collins, Uhlenbruck, & Rodriguez, 2009; Oliver, 1997). Among the most important organizational structures that facilitate misconduct are those that enable the selection of employees who are receptive to engaging in misconduct or who are susceptible to the types of social-influence processes that draw people into misconduct (e.g., those who have internalized the norm of obedience to authority).

In the *socialization stage*, new organizational participants are exposed to the techniques and attitudes that support the wrongful course of behavior. Schein (1961) characterizes socialization process as composed of three phases: unfreezing, change, and refreezing. In the unfreezing phase, new organizational participants are stripped of their old identities. In the change phase, new organizational participants incorporate their new identities through exposure to role models with whom they can identify and to situations that facilitate internalization. In the refreezing phase, new organizational members are placed in environments that reinforce their new identities. In the abstract, socialization and selection are alternative mechanisms for insuring that new employees function effectively in a corrupt work environment, although, in reality, they likely work hand in hand to accomplish this objective.

Palmer (2008) has extended the four-stage model in three ways that are compatible with the model's underlying logic. He contends that misconduct need not start at the top of an organization, but can be initiated by middle managers and lower-level employees. He identifies a range of additional social psychological processes (such as the generalized norm of reciprocity) and organizational structures (such as scripts and schemas) that can facilitate the proliferation of misconduct. Finally, he maintains that there are a number of variables that regulate the extent to which misconduct spreads throughout an organization. Whereas Brief et al. (2001) and Ashforth and Anand (2003) imply that the process through which misconduct becomes an organizational phenomenon is inexorable, Palmer contends that the process is more problematic and ultimately tenuous.

Work on the process by which organizations become corrupt is growing, with an eye to developing ways to thwart its emergency, categorize its manifestations, and recover from its occurrence (Ashforth, Gioia, Robinson, & Trevino, 2008; Lange, 2008; Misangyi, Weaver, & Elms, 2008; Pfarrer, Decelles, Smith, & Taylor, 2008; Pinto, Leana, & Pil, 2008). All of this work shares a common theme; it provides one answer to the often-posed question, "why do good people do bad things?" This model suggests that misconduct proliferates throughout an organization largely through processes that can be considered mindless (Langer & Moldoveanu, 2000; Weick & Roberts, 1993) or have what Cialdini (1993) calls a "click whirr" character. For example, employees follow the orders of superiors who possess legitimate authority without considering the merits of the orders themselves (Milgram, 1965). And employees mimic the behavior of co-workers without considering the rationale for that behavior (Bandura, 1977). The fact that a superior has issued an order and the fact that a co-worker has perpetrated a behavior is sufficient to cause an employee to follow the order and engage in the behavior him/herself.

*Spread of misconduct in industries, fields, and economies.* The spread of misconduct among organizations may at first appear to be identical to the spread of misconduct within organizations, only applied over a broader set of actors, but to us the differences are noteworthy. Organizations are "strong" social systems with a number of homogenizing characteristics: lengthy tenure and significant time commitment, uniform socialization of newcomers, and leaders with formal authority, including control of rewards such as salary and promotions. Within organizations, the spread of misconduct that a manager appears to condone or encourage is an overdetermined outcome: there are multiple explanations that can be difficult to distinguish. Between organizations, formal-authority relations are rare, control of rewards is indirect at best, and interactions generally occupy less of the individual's time (though some inter-organizational relations have long tenures). Thus the explanation of the spread of misconduct across organizations necessarily involves a smaller set of plausible accounts.

There is currently little research that examines the proliferation of practices that meet the strict definition of misconduct that we embrace. There is, however, research on the spread of borderline practices, which most would consider unethical and that some would consider counter-normative. This work locates the causes of the proliferation of misconduct in the interplay between institutionalization in the organizational field and localized pockets of deviance. For example, Westphal and Zajac (1994) examined symbolic management of shareholder concerns through the announced adoption and subsequent non-implementation of performance-contingent pay plans for CEOs. While most corporate governance reformers considered performance-contingent pay plans important tools for aligning the incentives of stockholders and CEOs, later adopters of such pay plans were decreasingly likely to actually implement them, and hence to claim one set of governance practices while using another. This behavior encroaches on stockholders' right to free consent, and approaches a violation of SEC rules of accurate disclosure. A later study of the announced adoption and subsequent non-implementation of stock buyback plans gave an even clearer depiction of the process, as it showed that non-implementation was particularly likely when the adopting firm shared directors with other firms that had adopted stock buyback plans but not actually implemented those (Westphal & Zajac, 2001). Hence, the unimplemented stock buyback plans—another unethical behavior that approached violation of SEC reporting regulations—spread through a network of directors. This offers an interesting duality, whereby imitation is involved both in the original adoption and implementation of a practice and in the subsequent illegitimate adoption of the practice without actually implementing it.

Imitation was also involved in the spread of poison pills and golden parachutes in the 1980s, which gave boards of directors a difficult task of judging the appropriateness of two different reactions to the threat of corporate takeovers (Davis & Greve, 1997). Both practices were favored by management, but their adoption depended on the norms of directors, who tended to view poison pills as a legitimate means of protecting the integrity of the firm against breakup, but were suspicious of golden parachutes as an apparent gift to failing managers. Hence, there was concern that adopting golden parachutes might violate stockholders' rights, and they spread slowly through imitation of firms headquartered in the same location rather than through the broader network of directors. The ability of local elites to form their own norms, contrary to the broader norms of the field, is a likely cause (Davis & Greve, 1997). Finally, the best evidence of misconduct spreading through imitation was the spread of option backdating through the board interlock network (Bizjak et al., 2009). This practice is under scrutiny by three federal regulatory agencies because it violated disclosure requirements to stock owners, underreported firm expenses, and failed to report taxable income for its officers. Because option backdating was not a publicly known practice, it spread covertly, and hence is an example of influence and secrecy influencing misconduct in networks, as discussed above.

A good account of these findings is that organizational decision makers experience uncertainty about the exact interpretation of rules and norms (Edelman, 1990). Faced with such uncertainty, they engage in sensemaking that relies heavily on social proof (Cialdini, 1993; Weick, 1995). Hence, they become more likely to do what has been done by others, especially those who are so proximate that the focal decision maker can observe the action and also get a first-hand explanation of its rationale (Davis & Greve, 1997). This account does not assume that misconduct becomes taken for granted like an established institution (Meyer & Rowan, 1977) or institutional logic (Thornton & Ocasio, 1999). The localized spread of the misconduct contradicts this interpretation. Rather, the decision makers are engaged in an exercise of testing the boundaries of a rule or norm against certain behaviors. The reason for testing the boundaries is almost always that it is beneficial for them to do so, so individual rationality (or at least, reward) has a role in their action; social proof takes over, however, when they seek to explore what they can get away with, leading to localized pockets of deviance.

## The Social Construction of Misconduct

As the expression goes, "it takes two to tango." Organizations cannot engage in misconduct unless a line is drawn between acceptable and unacceptable behavior, and organizational behavior is evaluated with respect to its relationship to that line; that is, unless judgments of misconduct are made by comparison to laws that have been written, ethical principles that have been promulgated, norms of social responsibility that have been elaborated, and conformity to each of these standards has been monitored and enforced. While many organizations and individuals claim to draw the line between acceptable and unacceptable organizational behavior, and attempt to monitor and control organizational behavior, we focus exclusively on social-control agents' activities. Social-control agents are entities that can make reasonable claims to represent the interests of broad communities of actors, and have capacity to monitor and enforce organizational behavior. These are the line-drawers, monitors, and enforcers to which organizations must, from a practical standpoint, pay the most attention. As noted in the introduction, we focus on social-control agents that are formally chartered to represent large constituencies, and that possess legitimate and effective means of monitoring and enforcing organizational behavior, such as governmental bodies or professional associations. Our arguments may, in part, apply to social-control agents that can make less reasonable claims to representativeness and possess less legitimate and effective means of monitoring and enforcement, such as rating agencies and the press.

*How Social-Control Agents Create Organizational Misconduct*

Social-control agents can create organizational misconduct directly. Perhaps most obviously, social-control agents can move the line demarcating acceptable from unacceptable behavior. For example, the passage of the Cellar–Kefauver Act in 1950 strengthened the U.S. antitrust regime such that many types of vertical and horizontal acquisitions that had previously been considered legal were rendered illegal. As a result, many firms found themselves in violation of U.S. antitrust law after the Cellar–Kefauver Act was passed, despite the fact that their behavior had not changed, simply by completing the same types of acquisitions that were legal before the Act was passed. Social-control agents can also create misconduct by changing the enforcement of the line between acceptable and unacceptable behavior. Although the Cellar–Kefauver Act was passed in 1950, the Federal Trade Commission (FTC) and the Justice Department only began enforcing this law vigorously in the early 1960s. Thus many firms found themselves pursued by the FTC and the Justice Department for completing acquisitions in the mid 1960s that had escaped these agencies' attention just a few years before.

The impact that social-control agents can have on the enforcement of the line between acceptable and unacceptable behavior can be subtle. For example, social-control agents can influence the propensity of third parties to come forward with evidence of an organization's misconduct. In 1996, TAP Pharmaceutical's marketing director, Douglas Durand, became uncomfortable with the company's sales practices in connection with its drug Lupron (Haddad & Barrett, 2002; Rogers & Weinstein, 2002; Weinberg, 2005). Durand left the company and filed suit on behalf of the federal government, contending that TAP engaged in a broad range of illegal marketing activities. The suit resulted in a negotiated settlement in which TAP agreed to pay $885 million in fines. TAP might never have been sued and punished for its marketing practices though had it not been for recent changes in the law designed to encourage whistle-blowing. *Qui tam* laws allow private citizens to file civil suit against companies on behalf of the federal government. The U.S. *qui tam* law, written during the Civil War, was modified by Congress in 1986 to increase a private citizen's cut of any financial judgment against a defendant from 10% to 30%, and to reduce the threshold of guilt to include "deliberate ignorance" or “reckless disregard” of regulations. Durand’s cut of the $850 million settlement against TAP was $126 million. It seems reasonable to assume that Durand would have been less likely to endure the seven years of investigation and court proceedings needed to complete the case against TAP without the promise of this sizeable payoff.

This discussion implies that social-control agents are linked to organizational wrongdoers in a relationship. The nature of the relationship between social-control agents and wrongdoers at the individual level is treated by a sociological approach known as labeling theory (H.S. Becker, 1963; Lemert, 1951; Schur, 1971). We draw on this theory to articulate the relationship between social-control agents and organizational wrongdoers, and in the process indicate how social-control agents can facilitate organizational misconduct in several indirect ways.

Labeling theorists distinguish between two types of misconduct: primary deviance and secondary deviance (H.S. Becker, 1963; Lemert, 1951; Schur, 1971). Primary deviance denotes wrongdoers’ initial rule-breaking behavior. Secondary deviance, in contrast, denotes wrongdoers’ subsequent additional rule-breaking behavior, which is largely formulated in reaction to the anticipated or actual reaction of social-control agents to their primary deviance. Labeling theorists believe that much of what we perceive as misconduct is secondary deviance, the result of the fear or actual labeling of other prior behavior as deviant.

Social-control agents can facilitate organizational secondary deviance in at least two ways. First, social-control agents can facilitate organizational misconduct that resembles secondary deviance by promulgating rules that provide opportunities for and, in extreme cases, even require organizations to engage in misconduct. For example, California instituted a labyrinth of ill-conceived rules as part of its attempt to deregulate the public power industry that made it easy for Enron and other energy companies to formulate schemes to manipulate the state’s energy markets (McLean & Elkind, 2003). Similarly, Ohio passed complex administrative rules that made it difficult for drugstores to be reimbursed for medications, leading one drugstore chain to file false claims to offset compensation claims they saw as having been unfairly denied (Punch, 1996, pp. 114–122). These examples provide field-level confirmation of Greenberg’s (1990, 1993) experimental results, which show that individuals are more likely to steal when organizational structure both creates systems perceived to be unfair and enables misconduct through lax controls. Second, social-control agents can facilitate organizational misconduct that resembles secondary deviance by motivating organizations to engage in behavior that reduces the risk of detection of and/or punishment of their involvement in other misconduct. For example, Arthur Anderson was famously prosecuted for shredding documents thought to contain evidence of its role in facilitating Enron’s fraudulent accounting practices (Eichenwald, 2005).

Labeling theorists also contend that when social-control agents create misconduct, they simultaneously create wrongdoers; that is, they transform rightful persons into wrongful ones. When social-control agents push individuals into secondary deviance by intrusive checking, they cause the individual to develop a deviant identity; that is, it causes them to think of themselves and act as wrongdoers. Thus labeling theorists believe that much rule-breaking behavior is the result of labeling individuals as wrongdoers.

Social-control agents can cause individuals to develop deviant identities by leading them to develop outlooks, establish relationships, and engage in behaviors that protect themselves from the psychological and practical impacts of the wrongdoer label (Crocker & Major, 1989; Goffman, 1990), and to search for and embrace techniques of neutralization that justify and thus cement their involvement in misconduct (Ashforth & Anand, 2003; Coleman, 1995; Coleman & Ramos, 1998; Gellerman, 1986; MacLean, 2008). Furthermore, social-control agents can cause individuals to develop associations with others who can provide resources that help them avoid detection and punishment. These associations can create networks that facilitate misconduct through mutual support and group pressures that shape members' norms, values and beliefs, and assumptions about the world (Ashforth & Anand, 2003; J. Collins et al., 2009).

The capacity of social-control agents to create organizational misconduct is, as illustrated above, evinced partly in the way in which the position of the line separating acceptable from unacceptable behavior varies over time and across places. The changing location (and often blurry character) of the line separating right from wrong is important in its own right; namely, it generates uncertainty about the precise location of the line separating acceptable from unacceptable behavior. This increases the likelihood that managers and organizations will accidentally cross the line between right and wrong (because they are not exactly sure where the line is located). Further, it causes managerial behavior near the line to be associated with risk, and hence selected primarily by managers and organizations under strain. It also leads to inconsistent enforcement, which can cause managers to speculate about the reasons for apparently arbitrary differences in treatment, possibly leading to suspicions of favoritism. Hence, uncertainty regarding the location of the line separating right from wrong turns social control into a risk-taking opportunity, and can lead to joint legitimacy loss for organizations and the agents who seek to control them.

### *The Determinants of Social-Control-Agent Behavior*

If one wants to understand fully the causes of organizational misconduct, one must understand the factors regulating where social-control agents draw the line between right and wrong, and how vigorously and successfully they enforce it. From an academic perspective, understanding those factors is half the story behind misconduct; yet from a practical standpoint, understanding the factors that shape social-control-agent behavior can allow one to forecast changes in the position of the line between right and wrong—a matter of substantial importance to managers. The study of social-control-agent behavior, as it pertains to illegal behavior, has been addressed by sociologists for some time, beginning with Black's (1976, 1998) general theory of the prevalence of legal rules in society. We briefly review one popular theory of social-control-agent behavior: conflict theory.

Conflict theory is based on two premises (R. Collins, 1975; Coser, 1967). First, it assumes that the location of the line separating right from wrong and the vigorousness with which that distinction is enforced are objects of conflict between competing groups in society (e.g., labor, capital, consumers, etc.), which possess different interests regarding the position and enforcement of the line between right and wrong and different amounts of economic, social, and political power. For example, when Swedish government regulators placed Skandia AB's top managers under criminal investigation, it reflected the underlying (and preexisting) conflict between Skandia Life's stockholders and the parent company's executives (Jonsson, Greve, & Fujiwara-Greve, 2009). Second, conflict theory assumes that the state, the primary social-control agent in the legal system, behaves in ways that reflect two fundamental facts. The state represents the balance of power among interest groups in society, and thus tends to represent the interests of the most powerful groups in society. Furthermore, the state is an actor itself, with its own interests and capacities.

The fact that the state tends to represent the interests of the most powerful groups in society implies that the line between right and wrong will be drawn and enforced in a manner that is consistent with the interests of the most powerful groups. Hence, the Enron fiasco, which caused substantial losses to some of the nation's large financial institutions, resulted in fines, incarcerations, and important changes to the legal system (most importantly, passage of the Sarbanes–Oxley Act). The Prudential Bache debacle, in contrast, only harmed individual (and, in most cases, elderly) investors, and consequently resulted in only a few fines, no incarcerations, and no changes to the legal system (Eichenwald, 1996).

The fact that the state is an actor with interests and capacities implies that the state will draw the line between right and wrong, and enforce the line in a manner consistent with its own interests and capacities. Thus the state tends to react promptly and vigorously when it is injured, as was the case in the heavy-electrical-equipment price-fixing conspiracy of the 1950s. This complex scheme primarily damaged federal, state, and municipal governments who were the main purchasers of the electric transformers at the center of the price-fixing arrangements (Geis, 1977). The state also acts rapidly and forcefully when it stands to gain from action, as was the case in Boston's Big Dig ceiling collapse. By bringing legal action against the construction project's general contractor, it was able to obtain a sizeable judgment that was then used to offset the construction project's unexpected and politically embarrassing high maintenance costs (Estes & Murphy, 2008).

The state also acts when it is in a position to win, as was the case in its pursuit of TAP Pharmaceutical for fraudulent marketing practices. TAP settled the federal government's civil suit for a record fine. But TAP contended that it settled the civil suit because the penalty, as large as it was, was less than the amount of lost business with Medicare and Medicaid that it would have had to forgo had it fought the charges (Weinberg, 2005). State action may also reflect a balancing of its interests and capacities. Thus it would be interesting to investigate whether the state pursues offenders of intermediate size because they have fewer resources than large firms (and thus are easier to prosecute), but draw more media attention than small firms (and thus their defeat offers more promise to enhance enforcement officials' reputations). For example, it might be argued that the Department of Justice has been slow to point its finger at potentially culpable parties in the recent financial crisis because doing so might evoke a call for large-scale, systemic changes in the financial industry; in fact, a preliminary analysis of the high-profile prosecutions on the heels of the mortgage crisis reveal that regulators have pursued primarily the already-shamed executives of defunct institutions, such as Countrywide Financial and Bear Stearns.

These observations on the state's behaviors point to the central role of the agendas pursued by social-control agents more generally. While social-control agents are significant because of their ability to direct attention and enforcement actions toward specific wrongdoing or particular wrongdoers, they are seldom unmotivated agents. Indeed, social-control agents' choice of targets in both the detection and labeling of misconduct is often motivated by a combination of self-interest, organizational capacity, and opportunity. A social-control agent's choice of target may be affected by the desire to increase its win rate by pursuing the most egregious and easily understood cases of misconduct, or to raise its public profile by pursuing the most visible, largest, or highest-status wrongdoer. Thus an important gap in our understanding, where more research is needed, is in the analysis of more systematic evidence on how social-control agents choose their agendas.

### *Gatekeepers and the Media*

Conflict theorists assume that social-control agents act to protect objective interests, both the interests of the state and those of powerful groups in society. Others who embrace a social constructivist view, though, assume that social-control agents have limited attention capacity and are drawn to cases of (alleged) misconduct by individuals or organizations seeking to influence enforcement. The media play an important role in this alternative account because their reports antecede enforcement action by social-control agents or corrective actions by the responsible organizations (Fisse & Braithwaite, 1983; Molotch & Lester, 1974). The media has a central role in the social construction view because of its ability to create scandal. A key feature of a scandal is that it creates a common-knowledge situation in which everyone knows about an instance of misconduct, they know that everyone else knows, and everyone else knows that they know (Adut, 2005). This common knowledge is important because a social-control agent may choose to ignore misconduct that is not important according to its criteria, as long as it is not common knowledge, but has to act for fear of being seen as negligent when it becomes common knowledge. The power of the media lies in the fact that even if the misconduct is widely known, it is not common knowledge unless it is made public, and hence publication creates pressure to enforce it. Thus, through reporting, social-control agents lose their discretion to choose which instances of misconduct to pursue and which to ignore.

The role of publicity in directing the attention of social-control agents lies behind the effectiveness of consumer advocates such as Ralph Nader (1991), who used a book and subsequent publicity to question the safety of specific car designs, as well as the general approach to safety practiced by U.S. car makers. These tactics are now widely known, and advocacy organizations typically use some mixture of publicity and direct attempts to influence social-control agents. This was clearly displayed in the dispute between environmental organizations and the U.S. chemical industry, in which the role of social-control agents as a lever in influencing the industry was seen in both the industry's greater responsiveness to press coverage that blamed it for environmental problems (Hoffman & Ocasio, 2001) and in the environmentalists' use of civil suits to influence the courts directly (Hoffman, 1999). Media attention can strengthen the influence of other social-movement tactics, as seen in the greater responsiveness to consumer boycotts when these receive press coverage (King, 2008). The media is not a passive tool, however: reporting and editing news is a purposive activity that involves organizational and individual agendas (Molotch & Lester, 1974).

Combining the insights of conflict theory and social-construction theory, we see that social-control-agent behavior can thus be understood as the sum of two distinct processes. The first is a proactive process in which social-control agents advance and protect the interests of the state and the most powerful actors in civil society. The second is a reactive process in which social-control agents follow up on misconduct that has been made public to such an extent that an expectation of enforcement has been created, creating the opportunity for institutional entrepreneurs to intervene and pursue their agendas.

### Consequences of Misconduct

Much of the empirical work on the consequences of misconduct has tested the basic "crime and punishment" intuition, which suggests that discovery of misconduct has adverse consequences for the responsible organization and individuals, and not for anyone else. Because the judicial consequences of illegal conduct are a matter of law studies, organizational scholars have instead emphasized extra-judicial consequences such as punitive reactions by owners, interaction partners, or customers. The main finding in this arena is that discovery of misconduct does often have negative consequences for those transgressors that are caught (e.g., Frooman, 1997), although as our argument on social-control agents suggests and as Margolis and Walsh (2003) explicitly point out, many who engage in reprehensible and even unambiguously illegal behavior are never caught. This seems like a line of investigation that has few new insights to offer, but it has actually produced some valuable findings. One source of insights is findings showing that the reactions to misconduct are not as clean as basic intuition suggests, with punishment being used selectively against some responsible organizations but not others, or against innocent organizations that bear the adverse consequences of misconduct by others. The selectivity may stem both from competing definitions of what constitutes misconduct (e.g., Ronen, 2000), and from uneven attention to organizations. In addition, investigations into the severity of consequences can be used to test theories of organizational status or power, or of the attention and judgment of social-control agents or society more broadly. Investigations of the consequences of misconduct have examined consequences for the focal organization, its network ties, other organizations that may be associated with it by social-control agents or lay audiences, and finally its individual members.

*Consequences for the Focal Organization*

Empirical work on the consequences of misconduct for the focal organization is guided by rational-choice reputation theory and sociological-status theory. To date, this work has focused on the primary prediction that firms suffer greater consequences of reported misconduct the higher their reputation or status is before the misconduct is reported. Rational-choice reputation theory and sociological-status theory see an organization's reputation or status as a kind of capital that increases the value of its output. It follows that this capital must have some of the properties of rent-generating capital in general: it has some lower boundary where it produces no value at all, and it acts as a multiplier effect so that the organization gets more from a constant addition the more is in place already.

The implications that reputation and status theory hold for the study of the consequences of misconduct are far from fully explored. First, although reputation and status theory are consistent with the basic prediction elaborated above, both theories are also consistent with variations of this prediction that remain to be tested. For example, it is possible to argue for a prediction of a constant deduction in the reputation/status effect for the same type of misconduct regardless of the initial reputation, except for organizations whose reputation is already so low that they will reach a minimal reputation as a result. Thus the continuous prediction given above is not the only one possible based on these theories, although in practice, it is the one tested by empirical researchers. Second, status theory allows that status is based on both an organization's quality and on its relationships with other organizations, but does not theorize how audiences weigh information about performance or quality sources of status, which are influenced by misconduct, relative to relational sources of status, which are not directly influenced by misconduct. In empirical work, an additive function of relational status and actual quality is often applied (Benjamin & Podolny, 1999). Despite these theoretical ambiguities, empirical work has proceeded and has yielded a largely consistent set of findings.

Much research is motivated by the desire to explore the impact of actions on an organization's reputation in areas directly related to the actions. For example, research shows that quality problems are more consequential for firms that have higher quality reputations to begin with, which is consistent with a model of specific reputations for quality being affected by measured quality outcomes (Barber & Darrough, 1996; Rhee & Haunschild, 2006). These studies used product recalls in the auto industry as the indicator of quality problems, and showed effects on market share (Rhee & Haunschild, 2006) and stock-market reaction (Barber & Darrough, 1996) respectively. A product recall is not necessarily a form of misconduct as we define it, but the corresponding prediction for misconduct would be that misconduct is especially damaging for firms with reputations that are based specifically on high ethical standards.

Other research is motivated by the desire to explore the impact of misconduct on an organization's general reputation, which can be defined as its evaluation across a range of socially valued outcomes such as quality, efficiency, or honesty. This research assumes that one form of misconduct can affect the focal firm in unrelated areas of activity by reducing the general reputation. Following this line of thinking, scholars of law and organization have been interested in extra-judicial punishment of organizational misconduct. Conceptually, the consequences of economic crime can be divided into the legal punishment and the reputation consequences, with the latter measurable as loss in stock value beyond what can be explained by fines and restitution. Alexander (2008) presented an interesting set of findings related to stock-market consequences of federally prosecuted instances of fraud, which support a theory of general reputations. First, the consequences are on average larger than the fines imposed by courts. Moreover, they are larger when: the victim has business ties with the perpetrator than when the victim is a third party; the offending firm is small and has only one line of business; and the record shows that adjustments in the firm or on the customer's side happened (e.g., when managers were terminated or contracts were lost). Further, the greater cost of defrauding customers indicates that, as expected, harm to a specific reputation is more consequential than harm to a general one.

Findings in support of general reputations have also been obtained in a study of how fraud in defense procurement led to stock-market penalties (Karpoff et al., 1999). This study also found that less powerful players in defense contracting were punished more harshly by the stock market for procurement fraud than more powerful ones. This result might provide a clue as to why Alexander (2008) found that smaller firms were punished more harshly than larger ones, a result that would appear to contradict reputation theory, because one's status and firm size are positively correlated, which would suggest that larger firms should be more strongly affected instead. Karpoff et al.'s (1999) finding that more powerful firms were less affected suggests that market power has a countervailing effect: although larger firms potentially have a greater reputation effect, lack of alternatives may protect them from the adverse consequences of misconduct.

A similar finding is obtained in studies that rank organizations by the status of their social relations; some organizations may be less discreditable than others despite their association with organizational misconduct because of their symbolic positions within the social structure (Wiesenfeld et al., 2008). Although some have found that status exposes actors to greater potential denigration (Adut, 2005; Phillips & Zuckerman, 2001), others have shown that actors who are well connected (Adler & Kwon, 2002; Granovetter, 1973) and have high status (Westphal & Khanna, 2003) may be protected from stigmatization because of the influence, solidarity, and information inherent in their social positions (Adler & Kwon, 2002; Burt, 1997). Organizations with high status or influential boards (Davis, Yoo, & Baker, 2003) and with close ties with influential others (D'Aveni & Kesner, 1993; Westphal, 1998) are able to draw on their networks when faced with negative organizational outcomes (Wiesenfeld et al., 2008). Better networked organizations can rely on their connections to disseminate information that contradicts the stereotyping and attributions central to the process of stigmatization (Wiesenfeld et al., 2008), resulting in fewer consequences for higher-status and more central organizations.

There is also a cognitive account for the prediction that high-status organizations would be less affected by reported misconduct if it were not directly relevant to the focal exchange. One version of status theory suggests that confirmatory biases (e.g., Nisbett & Ross, 1980, pp. 181–182) create inertia in status rankings in organizations that have high-status connections, such as directors with high social capital (Wiesenfeld et al., 2008; Yu, Sengul, & Lester, 2008). According to this argument, reports of misconduct by a high-status actor may be considered implausible or irrelevant to the focal exchange. High-status actors are generally perceived as more competent, credible, and trustworthy than their lower-status peers (D'Aveni, 1990; Geis, 1977; Giordano, 1983), and thereby thought to be less likely to have committed misconduct.

In addition, status and social capital may engender positive affect (Wiesenfeld et al., 2008; Zajonc, 1980) that counters the negative affect-laden attributions inherent in stigmatization (Devers, Dewett, Mishina, & Belsito, 2009), and thus helps observers rationalize the behavior of high-status actors. It may also direct attention toward positive aspects of the firm or downplay the importance of the discrediting revelation (Masten, 2001; Rhee & Valdez, 2009). Finally, others may be disinclined to punish elites for their infractions, although their excuses are no better received than their lower-status peers (Ungar, 1981). These arguments on high-status isolation are consistent with the theory of middle-status conformity, which posits that middle-status firms are most constrained because they have more status to lose than low-status firms but a smaller cushion of audience belief preservation than high-status firms (Phillips & Zuckerman, 2001). A test of this argument would involve a prediction of an inverted-U-shaped effect of status on the punishment following reported misconduct and data on firms from a wide range of status positions.

Despite this considerable amount of research, puzzles remain. Perhaps most importantly, some findings that favor a theory of general reputations seem to contradict the theory of high-status isolation. For example, it has been shown that high-status actors such as celebrity CEOs are subject to high expectations, which may lead to exaggerated consequences when expectations are violated (Khurana, 2002; Wade, O'Reilly, & Pollock, 2006). Studies demonstrating this effect have used samples of firms of mid to high status, and, in such data, high-status firms should experience less negative consequences if the theory of high-status isolation were to apply to this outcome. The finding of a positive relation instead supports the theory of general reputations that are affected more severely when the original reputation is high.

### *Consequences for the Network of the Focal Organization*

Earlier we mentioned that the theory of relational status posits that links to other social actors are sources of status (Podolny, 1993, 1994, 2005). If misconduct only harms quality judgments and not relations with other actors, it will not affect relational status. However, such a narrow effect seems unlikely: if the misconduct is related to a specific reputation then customers are likely to leave (Alexander, 2008; Rhee & Haunschild, 2006). High-status organizations can easily initiate new exchange relations (Baum, Shipilov, & Rowley, 2003; Stuart, 1998), suggesting that departures will be disproportionately from the high-status range of customers, thus reducing the relational status of the organization. A similar argument holds for misconduct that harms general reputations.

The same prediction has also been made based on stigmatization processes, where actors avoid association with anyone who has been labeled negatively. In the stigmatization of individuals, status appears to be a liability because it gives rise to visibility, which increases the likelihood of isolation (Pontikes, Negro, & Rao, 2008; Pozner, 2007). Likewise, organizations with visible ties to an organization with a reported case of serious misconduct limit their exposure by cutting off ties to it (Jensen, 2006; Sullivan, Haunschild, & Page, 2007). Although this behavior may be motivated by fear that they may become victims of future misconduct, it is not farfetched to interpret the action as an attempt to avoid being dragged down by the status loss of their exchange partner. In other words, managers behave as if they subscribe to a theory of relational status, and thus view other organizations as less valuable ties when they lose their status. Research on declining organizations is consistent with this speculation. It shows that organizations in decline have difficulty maintaining exchange relations, including relations that are seemingly risk free for the counter party such as purchases that are paid on delivery (Sutton, 1990).

*Consequences for Other Organizations*

There is evidence suggesting that reported misconduct harms organizations other than the original perpetrator. The mechanism behind this effect is categorical delegitimation, a further extension of the general-reputation idea treated above. While general reputation within a single organization means that misconduct in one area of activities (e.g., top-management compensation) may reduce evaluations in other areas (e.g., product quality), categorical delegitimation means that misconduct by one organization may taint other organizations seen as similar to it (Jonsson et al., 2009). This happens because individuals use schemas to form beliefs about social actors such as organizations (e.g., Tajfel & Turner, 1986; Turner, 1985), and this use extends to judgments on trustworthiness and reliability. Hence, when an organization commits misconduct, audiences may not only judge that it is likely to do so again, but also conclude that similar organizations are likely to commit misconduct. This theory is similar to the theory behind organizational legitimization through categorical judgments (Dobrev, Ozdemir, & Teo, 2006; Hannan, Polos, & Carroll, 2007), but, in the case of misconduct, the generalization to the category transmits delegitimating information instead (Jonsson et al., 2009). How far categorical delegitimation will spread is an unresolved question, but firms need not be formally linked to suffer the effects of stigma by association. Reactions to financial misconduct, such as customer loss and stock-value loss, have been found to spill over to unrelated firms with shared characteristics (Da Dalt & Margetis, 2004; Jonsson et al., 2009; Xu, Najand, & Ziegenifuss, 2006).

Some work has reported that the delegitimating effects of reported misconduct can spread very widely. In one study, the press reported that top managers illegitimately extracted rewards such as incentive payments and low-cost apartments for relatives from the Swedish insurance firm Skandia, which caused central social-control agents (notably, prosecutors) to act against the firm (Jonsson et al., 2009). The press reports alone were enough to affect sales of mutual funds marketed by other insurance firms, as well as mutual funds marketed by firms of similar size and market niche as Skandia, even if they were in unrelated businesses (Jonsson et al., 2009). Thus misconduct affected other firms of the same organizational form (i.e., insurance firms), but also firms that had other organizational forms (e.g., banks or pension funds) but superficial similarities with the organization responsible for the misconduct. This extent of the spread is remarkable because this investigation involves a general reputation spreading across organizational forms; after all, managerial self-enrichment is not directly related to product quality, so a case could be made that this misconduct should not even have affected the market share of Skandia, where the misconduct took place.



### *Consequences for Individuals within the Organization*

Another constituency that may suffer consequences from organizational misconduct is the organizational elite. Currently, there is no theory that explicitly addresses the link between organizational misconduct and organizational leaders' outcomes, although several economic theories can logically be extrapolated to address this question. According to the theory of *ex post* settling up, the consequences of organizational misconduct should be transferred to individuals through signaling (Fama, 1980; Fama & Jensen, 1983). Signaling theory holds that, given uncertainty and asymmetric information, information about quality, expectations, and performance can be gleaned through concrete actions and objective outcomes that serve as signals (Milgrom & Roberts, 1982; Shapiro, 1982; Spence, 1973). The theory of *ex post* settling up thus holds that organizational leaders are penalized for negative organizational outcomes or rewarded for strong performance on both internal and external labor markets, and that the penalties or rewards they receive will be commensurate with the strength of firm performance. By this logic, the leaders of firms engaging in misconduct will face labor-market penalties because the actions of the firms they oversee reflect their inadequacies (Lorsch & MacIver, 1989). This theory assumes that firm performance is a direct and accurate signal of leader quality, reflecting some underlying reality about leader skills, and that labor markets are rational, efficient information processors (Fama, 1980, p. 296). The consequences of misconduct on both internal and external labor markets may be even stronger for directors than for executives, as the board is ultimately responsible, by legal definition, for organizational misconduct (Gove & Janney, 2004; Meindl, Ehrlich, & Dukerich, 1985; Zahra & Pearce, 1989), and because director interlocks are channels through which information flows (Kang, 2008; Mizruchi, 1996).

Much research inspired by the theory of *ex post* settling up is devoted to exploring the impact of corporate performance and behavior on leader outcomes. This work demonstrates that external markets for directors do account for performance at the focal director's home organization, albeit imperfectly. In general, outside directors are better compensated and have more new offers of board seats when their firms perform well (Ferris, Jagannathan, & Pritchard, 2003; Yermack, 2004), but lose their positions when performance is poor (Yermack, 2004). Signals of sound corporate governance, such as rejecting anti-takeover provisions (Coles & Hoi, 2003) and forcing out underperforming CEOs (Farrell & Whidbee, 2000), also lead to longer tenure in existing board appointments and invitations to join new boards. Negative organizational outcomes, particularly those that signal declining firm performance, are found to dampen the future career opportunities of professionals at all levels of the organization (Hamori, 2007). In contrast, although outside directors cutting dividends at their home firms are more likely to lose seats on other boards, those directors experiencing poor performance at their home firms do not lose outside board seats (Kaplan & Reishus, 1990).

Recently, research inspired by the theory of *ex post* settling up has begun to explore the impact of organizational misconduct specifically. This work indicates that directors at organizations found to have committed illegal or illegitimate acts face significant labor-market penalties, losing both their positions at the misconduct firm (Arthaud-Day & Certo, 2006; Srinivasan, 2005) and seats on other boards (Srinivasan, 2005), although these effects may be moderated by intra-organizational political dynamics and the relative social position of both organizational elites and the misconduct firm itself (Pozner, 2007). Clearly, much more work along these lines still needs to be done.

More work also needs to be done on how organizational misconduct affects organizational members below the top management level, including individuals who are not implicated in the misconduct. Misconduct by the organization is most likely problematic for organizational members: indeed, perceived failure by an organization to engage in pro-social behaviors has already been shown to cause reactions from organizational members (Dutton & Dukerich, 1991). A promising approach for advancing research on individual consequences of misconduct is to conceptualize misconduct reports as a stain that threatens the identity of organizational members (Ashforth & Kreiner, 1999). It follows from this conceptualization that reported misconduct by the organization can generate individual identity-protection responses that range from denigration of the social-control agent seeking to punish the misconduct to withdrawal from the organization accused of misconduct.

## Discussion

### *Surprises in Research on Misconduct*

As we noted earlier, research on organizational misconduct occurs against the background of a strong set of commonsense intuitions. Research that proves them wrong is especially important because it can help us see misconduct differently. Although research attention to misconduct has been quite uneven, with some questions addressed much more often than others, it has delivered a number of conceptual advances and empirical surprises. Some of these are surprising enough to warrant additional research to confirm the findings and investigate the mechanisms underpinning them.

Intuitively, acts are labeled as misconduct whenever they are harmful or morally objectionable. We have defined misconduct as the result of interaction between an organization and a social-control agent, and we think it would be useful to investigate both sides of the relation as causes of misconduct. This insight is not unique or novel, but there is still limited empirical work on the actions of social-control agents. In our view, the exclusive focus on acts as being (obviously) either misconduct or not depending on some set of consistently applied norms is a conventional truth waiting to be overturned.

Intuitively, misconduct is done by bad people. Consistent with this intuition, there is a considerable amount of research that looks at individual-level differences (e.g., gender, age) that might be related to preference or value structures that are hypothesized to influence the likelihood of engaging in misconduct, especially unethical behavior (Tenbrunsel & Smith-Crowe, 2008). Although research indeed finds individual effects, the main theoretical and empirical thrust of the work reviewed here—even the work that focuses on the individual—focuses on the individual's responsiveness to the environment rather than individual consistency. Certain organizational contexts appear to generate misconduct, certain locations in networks appear to generate misconduct, and certain situations (e.g., failure to meet goals) appear to generate misconduct. This should not be surprising; just as norms are tools of social control and hence more social than individual, misconduct is likewise more a social phenomenon than an individual one.

Intuitively, misconduct occurs in organizations that tempt their officers and employees too much and control them too little. This intuition is quite accurate in general, but it leaves out two important exceptions. First, it applies only to misconduct against the interests of the organization; when misconduct is instead on behalf of the organization and at its behest, stronger organizational control leads to more misconduct. This is the essence of the argument on cultures of misconduct, risk taking, and corner cutting. Second, at least in theory, intrusive social-control agents can create incentives to conceal borderline behaviors that ultimately cause organizations and individuals to fall into actual misconduct.

Intuitively, discovery of misconduct harms the responsible organization or individual, and leaves others untouched. Much research on status effects seeks to modify this statement rather than refute it, and there is some (although not enough) research suggesting that the reactions are indeed contingent on the identity of the perpetrator and the organizations with which it is connected. Through categorical delegitimation, innocent organizations also suffer the consequences of misconduct.

*A Final Thought about our Definition of Misconduct*

We have defined misconduct in relative terms. In our approach, behavior qualifies as misconduct when social-control agents consider it to be such. Others have argued in favor of defining misconduct in absolute terms (Tenbrunsel & Smith-Crowe, 2008). They contend that whether behavior qualifies as misconduct should depend on whether the behavior violates a researcher-defined standard, perhaps informed by the work of philosophers or theologians. We have discussed the social scientific pros and cons of our relativist approach, concluding that the pros outweigh the cons, and recognize that others might disagree with our pro/con calculus. Further, we suspect that some might favor the alternative absolutist approach for other, normative reasons (e.g., Sandelands, 2008).

Our field's founders argued that organization studies is an applied science and, as such, should be devoted to improving managers' abilities to achieve valued outcomes (Litchfield, 1956; Thompson, 1956). Some who embrace this point of view contend that organization studies should improve managers' capacities to achieve a broad range of valued outcomes, including the eradication of wrongdoing (c.f. Bartunek, 2003; Boulding, 1957). Further, Khurana (2007) has documented that management schools have evolved from institutions pursuing what might be called a professionalization project to organizations pursuing what might be considered training objectives, in the process abandoning the pursuit of "higher ideals" in favor of producing "hired hands." Many have lamented this trajectory and called for management educators to impart values, as well as techniques, to their students.

As students of misconduct in and by organizations, we understand the impulse to infuse management research and education with values. Undoubtedly, like many others who study misconduct, we are drawn to this topic because we are disturbed by the level and impact of organizational misconduct in society, and we aspire to reduce the frequency and impact of organizational misconduct. However, we subscribe to a view articulated by Weber (1946) in his now-classic essay, "Science as a Vocation," that has been (sometimes derisively) called a "value-free" approach. We realize that the virtues of this approach as an overarching framework have been debated and important limitations of this approach have been identified (Pfeffer 1993, 1995; Van Maanen 1995a, 1995b). Nevertheless, we believe that a value-free approach affords greater freedom to explore the causes and consequences of organizational misconduct. Specifically, it allows us to develop an understanding of the ways in which behavior comes to be defined as misconduct. Moreover, we think that attempts to reduce misconduct will be more successful if informed by an understanding of how behavior comes to be labeled as unethical, socially responsible, and ultimately illegal.

*Future Research Opportunities*

Research on the individual-level processes related to misconduct is plentiful, but research on the connections between individual- and organization-level phenomena related to misconduct remains relatively undeveloped. The effect of strain on risk taking on behalf of the organization (McNamara & Bromiley, 1997) and fraud using the organization as a tool (Harris & Bromiley, 2007) is an interesting causal relation that has seen limited research so far, and is connected with the growing research tradition on effects of performance below aspiration levels in organizations (e.g., Greve, 2003).

Likewise, misconduct in networks is a topic that has yielded fascinating findings (Baker & Faulkner, 1993), but there is not enough research to give clear answers on what kinds of networks and network positions generate misconduct and why. A role of relatively isolated cliques is suggested by current evidence, but it is important to keep in mind that brokerage positions in networks give opportunities for information control (Burt, 1983), which in turn might facilitate fraud. Hence, there is ample opportunity for a rerun of the clique versus structural-hole debate in the domain of organizational misconduct. Also, only longitudinal studies of networks can answer the question of whether networks of actors engaged in misconduct take on forms that favor secrecy from the start, or whether this feature evolves over time.

A frequent dilemma in research on misconduct is that data become available when a social-control agent detects misconduct and decides to act against it. Research on organizational misconduct reports findings pertaining to the effects of variables such as size or economic performance on the likelihood that firms engage in wrongdoing. Interpretation of these findings is ambiguous, because we do not know the extent to which they reflect the likelihood that organizations will engage in misconduct or the likelihood that social-control agents will act against it. Developing a way to investigate the behavior of the organization and the social-control agent jointly could lead to breakthroughs in this research.

The literature on organizational accidents has displayed a number of conditions that lead organizations to commit misconduct apparently without intent, but some of the same conditions, such as fast-moving and complex processes that are poorly understood by nonspecialists, are also likely to be involved in misconduct. The concealment of trades by Nick Leeson at Barings Bank, for example, was only possible because of his isolation from headquarters and its poor understanding of his trades, and could only escalate to ruinous levels because of the speed of price movements and trades in financial markets. The mixture of accident and fraud in the Savings and Loan Scandal (Mezias, 1994) seems to be replayed in the current financial crisis, and one would hope that it provides an opportunity to make further progress on the relation between organizational accidents and organizational fraud.

In the research on detection of misconduct and *ex post* settling up, there seems to have been a strong focus on looking for "fair" kinds of settling up and insufficient attention to the exceptions: misconduct that is detected late and punished insufficiently. For example, in the wake of Al Dunlap's ouster from Sunbeam Corporation after the discovery of a "bill-and-hold" scheme to inflate booked sales, claims of misconduct at his earlier firms surfaced, although he had been a hero for the investment community right up to the point of his fall. The striking difference between contemporaneous and *post hoc* evaluations of his performance is not unique, and seems to go beyond the status effect of bad news shown in celebrity CEOs (Wade et al., 2006). More research is needed on such effects, which could be some mixture of contemporaneous hero worship and vilification after misconduct has been reported.

Related to *ex post* settling up, it has been found that customers exit from innocent organizations that are cognitively categorized as similar to an organization involved in reported misconduct (Jonsson et al., 2009). The potential implications for such an effect are large because of the way stigmatization and categorical delegitimation expands the damage from misconduct, and the resemblance to the contagion effects in financial panics is suggestive. It seems like an effect that may also be found at higher levels of analysis (such as industrial or financial categories) or lower ones (such as CEOs).

## Conclusion

News about the financial crisis of 2008–2009 has contained enough traces of misconduct to once again spur researcher interest in this topic, so it is easy to predict that there will be an upswing in research on misconduct. Whether this upswing will lead to important contributions depends on the lessons that those who enter the field learn from past work, and how they apply these lessons to identify promising areas of contribution. Although research on misconduct is responsive to the news cycle, it has deep enough roots that it is past the phase of pure exploration. A number of theories formulated at different levels of analysis have been proposed for both the causes and consequences of misconduct. Some of these theories have been fruitful empirically; others have been less successful; yet others have seen little or no testing.

We have sought to review the current literature, make suggestions on promising areas of work, and propose some corrections to current work. The review and proposals are subjective even when three authors collaborate, but for what it is worth, we think there are some very obvious opportunities to make significant contributions to our knowledge on organizational misconduct. Most likely, there are also opportunities that are less obvious to us, so we expect our recommendations to err by omission rather than by commission.

The potential for contributions that we have not identified here, however, only strengthen our main message: much work remains before we have a good understanding of organizational misconduct. We hope that one silver lining in the recent economic troubles is better availability of data to test theories of misconduct empirically. Researcher interest is high and theoretical ideas are already in place, so data collection will be the main constraint in advancing research.

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