

**Stock Market Responses to Unethical Behavior in Organizations:
An Organizational Context Model**

Abstract

We develop and test a model that extends the understanding of how people react to news of organizational unethical behavior and how such reactions impact stock performance. We do so by taking into account the interplay between the features of specific unethical acts and the features of the organizational context within which unethical acts occur. We propose a two-stage model in which the first stage predicts that unethical acts that benefit the organization are judged less harshly than are unethical acts that benefit the actor, when the organization is seen as pursuing a moral goal (e.g., producing inexpensive medicine rather than tobacco products). In such cases, the motives behind the unethical act are construed as an individuals' intentions to pursue a moral end. The second stage of our model connects moral judgment to action against the organization as a whole. We propose that moral judgments of an unethical act are more likely to translate into negative economic consequences for the organization when the unethical act is seen as benefiting the organization, because in such cases the organization is construed as an accomplice. Study 1 is an event study of stock market reactions to organizational unethical behavior in which the features of organizational unethical behavior were operationalized by coding media coverage of unethical acts. Study 2 is an experiment that used news stories to manipulate features of unethical behavior and measured participants' estimates of stock performance, while incentivizing participants for accuracy. Both studies found support for our model.

Keywords: unethical behavior, moral judgments, stock performance

UNETHICAL BEHAVIOR IN CONTEXT

Stock market responses to organizational unethical behavior can determine the fate of firms (King and Soule 2007), industries (Jonsson et al. 2009), and economies (Lounsbury and Hirsch 2010). Extant models of responses to unethical behavior lead to general predictions that these acts will have negative implications for stock prices due to anticipated negative reactions by external stakeholders (Gunthorpe 1997, Paruchuri and Misangyi 2015, Rao and Hamilton 1996). This view ignores tremendous variance in responses to unethical acts occurring within organizations, as the same unethical act often results in very different reactions by the stock market. For example, both Whole Foods and Exxon had news stories published where the organizations were overcharging customers; while Exxon experienced a three percent drop in stock price following the story, Whole Foods saw a one percent *increase*. Current models are limited in their ability to explain such differences in stock market responses. We argue that this is the case because they tend to conceptualize unethical behavior as conducted either by the organization as a whole, acting collectively as a singular agent behind the unethical act (e.g., Davidson et al. 1988, Gunthorpe 1997, Paruchuri and Misangyi 2015), or by individual agents acting in isolation from the firm context (e.g., Alicke et al. 2008, Lerner et al. 1998).

We extend past perspectives by proposing that stock market responses to organizational unethical behavior are shaped by an interplay between features of individual unethical acts and features of the organizational context within which the acts occur. Our premise is that since investors are focused on the likelihood that publicly traded firms will return a positive investment, they are sensitive to the possibility that unethical acts may lead to negative reactions by the public; for example, in the form of consumer boycotts or legal sanctions (Gunthorpe 1997, Lindenmeier et al. 2012, Palmrose et al. 2004). Thus, to understand how investors respond to organizational unethical behavior, it is important to understand how people form moral judgments of unethical acts that transpire within organizations, as well as whether these judgments translate, or are anticipated to translate, into actions that are economically damaging to the firm as a whole.

We propose a two-stage model that focuses on attributions of *a perpetrator's motives* as a determinant of moral judgments directed toward the *individual agent(s)* who perpetrated the act (stage 1) and attributions of organizational responsibility as a determinant of whether moral judgments of the act translate into consequences for the *organization* (stage 2). Our model is consistent with dominant

UNETHICAL BEHAVIOR IN CONTEXT

ethical decision-making frameworks suggesting people first have to notice a moral issue, then formulate judgments about it, and these judgments in turn guide their reactions (Jones 1991; Rest 1986). To construct our model, we build on a distinction between unethical acts as either benefiting the firm (pro-organizational unethical behavior, such as overcharging customers to benefit the firm) or an isolated individual (or group) who committed the act (pro-self unethical behavior, such as stealing from the organization to benefit the actor) (Pinto et al. 2008, Umphress and Bingham 2011)¹. This distinction is crucial to both stages of our model.

In the first stage, advancing self-interest by harming others through unethical acts (pro-self unethical behavior) will generally be judged as immoral, as it represents a clear-cut violation of a community's interests (Fehr and Gächter 2000). However, an unethical act that is intended to benefit the firm (pro-organizational unethical behavior) may represent a conflict of one goal valued by the community against another. For example, accounting irregularities aimed at helping a firm produce affordable medication may undermine the value of transparent reporting, but with the socially-valued goal of improving public health. Thus, when the overarching goal of the organization is perceived as more moral (e.g., producing affordable medication), pro-organizational unethical acts may be judged as less immoral than pro-self unethical behavior.

In the second stage of our model, concerning the connection between moral judgments of an individual agent(s) unethical behavior to consequences for the organization as a whole, we posit that whether the unethical act was pro-self or pro-organizational will inform whether the broader organization should be held responsible. Unethical behaviors committed by individual agent(s) within an organization are often ambiguous with respect to the degree to which the firm as a whole was involved and should be held responsible. When the unethical behavior is engaged in to benefit the organization, observers might suspect that the organization as a whole allowed or even facilitated such actions, and moral judgments of individual agent(s) unethical acts are likely to translate into actions

¹ In some situations an unethical act may be seen as helping the actor as well as the firm. Snyder (2010), for example, found that doctors were fraudulently using intensive care units to procure transplant livers, which was likely motivated by concern for the patient, while the physician and the hospital benefited by improving the number of successful transplants. However, it is likely that in most situations the actor and the organization are not seen as benefiting from unethical behavior to an equal extent, and our theory focuses on such situations in which there is one key perceived beneficiary of the unethical act.

UNETHICAL BEHAVIOR IN CONTEXT

against the organization. However, observers are less likely to suspect that the organization was involved when an employee engages in pro-self unethical behavior, which produces no benefit (or even produces harm) for the organization. In such cases, observers' moral judgments of individual agent(s) unethical acts are less likely to translate into negative consequences for the firm.

Thus, our model takes into account the interplay between the unethical act and the organizational context and reveals the crucial roles of intended beneficiary of the unethical act and the morality of the organizational goal in explaining stock market responses to unethical organizational behaviors. Figure 1 summarizes our theoretical model, which we tested and found support for across two studies. Study 1 is an event study of stock market reactions to organizational unethical acts. Study 2 is an experiment in which we used news stories to manipulate features of unethical behavior and measured people's estimates of stock price performance, while incentivizing participants for accuracy. Study materials, data, analysis code, online appendices, and other materials are available at:

https://osf.io/ke7ts/?view_only=13960157997041c2a04926b0a94ac791

[Insert Figure 1 approximately here]

This paper makes several theoretical contributions. Most extant models of responses to organizational unethical behavior conceptualize such acts as committed within a black box of the firm (Greve et al. 2010). We show the importance of opening this box and simultaneously considering the features of the act itself, as well as the features of the organizational context, to understand responses relevant to the entire firm. For instance, although past theories suggest that unethical behavior results in moral reprimand (Greve et al. 2010), we show that unethical behaviors committed within organizations may not result in negative responses (in the form of harsh moral judgment) in the cases of pro-organizational unethical behavior occurring in firms seen as pursuing a moral goal. Most past models of responses to unethical acts that occur within a firm also assume that negative reactions lead to negative responses for the entire organization (Karpoff et al. 1999, Strachan et al. 1983). We show that depending on the features of the unethical act, this might not be the case, most notably in situations where the act was meant to benefit the actor and not the firm.

We also extend recent work that has emphasized the importance of looking at the distinction between personal and social motives of similar unethical acts (Gino and Pierce 2009, Umphress et al.

2010, Wiltermuth 2011, Wiltermuth et al. 2013). Though this work has been important in clarifying the motivational differences arising as a function of different possible beneficiaries of unethical behavior, it was primarily intended to explain the reasons *why* people engage in other-benefiting unethical acts. Thus, it says little about how external stakeholders and the public *react* to unethical behaviors committed to benefit others versus the self, a question that our studies begin to answer.

Another contribution of our research is to prior work on factors that buffer an organization from negative economic consequences following unethical acts becoming public knowledge. Prior work in the area of corporate social responsibility (CSR) has shown that prosocial programs, such as sponsoring volunteer initiatives, produce a type of moral capital for a firm that provides shareholders with “insurance-like” protection in the event of unethical organizational acts (Flammer 2013, 2015, Godfrey et al. 2009, Pelozo 2006). We contribute to this work by identifying another organizational feature that in some cases produces “buffering effects,” irrespective of any CSR programs. Our model suggests that the morality of an organization’s goals also affords insurance-like protections when the unethical act benefits the organization, as in such cases moral judgments of the act and the resulting negative consequences for stock performance are tempered.

First stage: Attribution of motives and moral judgment of the unethical act

Moral rules serve to enable social life by ensuring that people do not harm others (Fehr and Gächter 2000, Haidt and Kesebir 2010). Not all moral rules aim to optimize the immediate good of the community, but generally, impressions of morality do depend strongly on the extent to which an action increases or decreases the wellbeing of larger social units (Brady 1985, Mill 1897). For example, Fritzsche and Becker (1984) presented a series of ethical dilemmas to a sample of marketing managers, and they found that the majority provided a rationale for their decisions by discussing consequences for the social welfare (e.g., “no significant harm to environment,” “risk of injury or death is low,” etc.). Similarly, in the well-known “trolley problem,” in which participants are asked to decide whether to flip a switch to redirect a trolley, thereby killing one person to save five, most people (90%) optimize the welfare of the community by flipping the switch (Hauser 2006).

Given the importance of community wellbeing in the perception of the morality of given acts, committing unethical behavior to satisfy one’s own self-interest by harming others will generally

UNETHICAL BEHAVIOR IN CONTEXT

be judged as immoral, because such behavior threatens the wellbeing of the community to benefit an individual (Fehr and Gächter 2000). However, organizational unethical behaviors can also be undertaken not to benefit the self, but to benefit a firm, and we argue that when the firm is pursuing a moral goal, moral judgments of pro-organizational unethical acts will be tempered. While some firms are focused exclusively on generating profit, and might not be perceived as pursuing a socially valued mission, others pursue a profit-maximizing and a pro-social mission simultaneously (Margolis and Walsh 2003). An example is a firm that produces inexpensive anti-cancer medication or a firm that pursues a triple bottom-line accounting framework. An example of a firm with a less moral goal would be a company that pursues profits while generating negative social externalities (e.g., tobacco companies such as Philip Morris and British American).² Given the importance of social impact in moral judgments, we propose that unethical behavior that benefits a firm pursuing a moral goal will be judged as less immoral than the same act occurring within a firm with less moral goals.

When a perpetrator commits unethical behavior to benefit a firm that is (also) serving a moral goal, the unethical behavior will be construed as an act that (also) helps the organization serve a socially valued goal and create social benefits, which should ultimately temper moral judgments of the act committed by the perpetrator. For example, if a company produces healthy and chemical-free food at competitive prices, and an employee engages in accounting irregularities, this sacrifices the value of transparency of reporting, but can be perceived as promoting a socially valued goal. For that reason, within organizations perceived as (also) serving a moral goal, the public may judge pro-organizational unethical acts as less immoral than pro-self unethical acts. For firms seen as serving less moral goals, the premium for an actor acting for the sake of the organization should be smaller, since the act is less likely to be construed as indirectly aiding a socially valued goal. Formally:

HYPOTHESIS 1: Pro-organizational (vs. pro-self) unethical behavior leads to more lenient moral judgments of the actor(s) the more the organization's goals are perceived as moral.

Second stage: Moral judgments of the act and stock market reactions

² Our conceptualization of the morality of an organization's goals resembles the notion of CSR (Godfrey et al. 2009), but represents a more general construct in that even when firms are pursuing their direct economic goals, these goals can still vary in the extent to which they generate social utility (e.g., a medical company pursuing only its direct economic interests versus a tobacco company pursuing only its direct economic interests).

UNETHICAL BEHAVIOR IN CONTEXT

Society is interested in responding to unethical acts by inflicting negative consequences on those responsible, since doing so maintains the social order (Fehr and Gächter 2000). For example, in the case of organizational unethical acts, negative public responses can take the form of legal sanctions (Simpson 2002), consumer boycotts (Miller and Sturdivant 1977), and lower willingness to invest in the firm (Frooman 1997), all of which should be reflected in a stock price decrease. As unethical acts performed by organizational agents are judged to be more immoral by the public (and investors anticipate the public to judge them as more immoral), stock performance should worsen.

At the same time, we argue that whether moral judgments of an unethical act translate into negative responses toward *the entire organization* (rather than the perpetrator) depends on the perceived beneficiary of the act, since the beneficiary serves as a strong cue for responsibility attributions. We specifically focus on responsibility attributions for the second stage of our model, which connects judgment to action, as there is much support from the moral and psychological literature regarding the centrality of such attributions in ultimate behavioral responses. For example, when discussing the notion of just desserts reactions, Darley (2009) concludes that it is moral culpability rather than harm that is mainly driving punishment judgments (Alter et al. 2007). Neural imaging research (Young and Saxe, 2009) also demonstrates the primacy of activation of brain areas that relate to theory of mind information, i.e., information that would help in understanding blameworthiness when deciding about punishment for moral wrongdoing.

Yet, organizational unethical acts are often ambiguous with respect to how much the firm as a whole was involved and should be held responsible. The central tension in agency theory illustrates this point: principals have an interest in monitoring agents within the firm, but in many cases agents act on their own, even against a principal's best interests (Eisenhardt 1989). For this reason, we argue that external stakeholders would attend to situational cues surrounding unethical behaviors to make sense of the extent to which the firm was involved. Following a similar logic, past work has focused on the extent to which an employee is in an obedient role as a situational factor explaining when third-party observers assign responsibility for unethical behavior to the actor rather than the organization (Hamilton 1986, Hamilton and Sanders 1995). If an individual is in an obedient position in the firm, it is less likely that third-party observers will believe that a broader organizational system was not

UNETHICAL BEHAVIOR IN CONTEXT

involved in an unethical act (Gailey and Lee 2005). This work suggests that while across a range of cases, observers might attribute responsibility for acts committed by individual employees to the firm, such attributions will be stronger in some cases (e.g., when the employee is in an obedient position). In a similar vein, we argue that the perceived beneficiary of an unethical act serves as an important cue determining whether moral judgments of the actor translate into negative stock performance.

Pinto et al. (2008) highlight the beneficiary of an unethical act as a key feature distinguishing when an act is seen as systemic to the firm (a “corrupt organization”) or simply carried out by an isolated member or group (an “organization of corrupt individuals”). Pinto et al. (2008) distinguish between an “organization of corrupt individuals, in which a significant proportion of an organization’s members act in a corrupt manner *primarily for their personal benefit*, and a corrupt organization, in which a group collectively acts in a corrupt manner *for the benefit of the organization*” (p. 688; emphasis added). Since there is no reason why a firm would entice unethical behavior that produces no benefit (or even produces harm) for the firm, external stakeholders should be less likely to suspect that the organization more broadly was involved when an employee engages in pro-self rather than pro-organizational unethical behavior. For example, observers are arguably more likely to perceive the firm as “guilty” of creative accounting that helped its profits than employee theft that harmed its profits. This is not to say, though, that external stakeholders, or investors, will not react negatively to pro-self unethical behavior (i.e., attributing that the firm cannot monitor employees), but to a lesser extent. Based on this logic, moral judgments of unethical acts are more likely to translate into negative stock market responses when the firm (rather than an isolated individual) benefited from the act. Formally:

HYPOTHESIS 2: The relationship between moral judgments and stock market response will be more negative the more pro-organizational the unethical behavior is perceived to be.

Overall model summary and areas of empirical ambiguity

Hypotheses 1 and 2 form a moderated mediation model (Figure 1), which leads to interesting implications for organizations within which unethical events occur. When the firm has less moral goals, in the first stage, pro-organizational unethical acts should be judged similarly negatively as pro-self unethical acts (as neither will be seen as promoting an ultimate moral goal of the organization). In

UNETHICAL BEHAVIOR IN CONTEXT

the second stage, these moral judgments should more strongly negatively impact stock market performance when the act is more pro-organizational, as in this case the organization is more likely to be construed as an accomplice. In firms with more moral goals, pro-self unethical behavior should in both stages elicit similar reactions as in firms with less moral goals, as the goal of the firm does not matter for how the unethical behavior is perceived. However, pro-organizational unethical behavior occurring in firms with moral goals presents an interesting and important empirical puzzle. In such cases, in the first stage, the unethical act committed by individual agent(s) will be judged less harshly because it will be construed as aiding a moral goal of the organization. However, in the second stage, if observers do form negative moral judgments of the unethical act, these moral judgments will translate into negative consequences for the firm given that the firm is likely to be construed as an accomplice. As such, it is unclear a-priori how the two stages combine and thus what the total effect of pro-organizational unethical behavior committed within organizations with a more moral goal will be. As the perceived level of morality of the organizational goal increases, observers might judge the unethical behaviors less harshly until a point at which such behavior is no longer encoded as immoral, effectively severing the link between unethical behavior and ultimate stock market performance.

Study 1: Event study

Study 1 is an event study of stock market reactions to organizational unethical behaviors. Our dependent variable was event-level cumulative abnormal returns (CAR) of stocks within firms where unethical behaviors occurred. To operationalize perceptions of morality of the organizational goal, and the beneficiary of the unethical act, we would ideally collect direct (self-reported) information on investors' perceptions of these characteristics of the unethical act and the firm. Given that such data would be nearly impossible to collect, we instead located newspaper articles describing organizational unethical behaviors, as this would be investors' main source of information concerning organizational unethical acts (Gunthorpe 1997). To approximate how an average investor would interpret the unethical act and how they perceive the firm in terms of the morality of its goals, we had trained research assistants (RAs) code each article for perceptions of these constructs. To validate our operationalization approach, we conducted semi-structured interviews with three institutional investors and two traders working in different U.S. banks. One investor captured a sentiment shared

UNETHICAL BEHAVIOR IN CONTEXT

by everyone we interviewed when he said, “No one really knows, fully, why stock prices vary in the way they do. And I don’t really care if price gouging is morally right or wrong, but the public might, and it’s more about what news of that actually does to the earning power of the firm. Market prices react very quickly and we are trying to anticipate how the public might respond and how that will impact earning power.” Information gathered from these interviews suggested that it was appropriate to operationalize perceptions of morality of the organizational goal and the beneficiary of the unethical act by measuring the relevant constructs from the perspective of the public.

Event sampling

Since the perceived morality of an organization’s goals may change over time (i.e., the morality of Enron’s goals prior to 2001 may be viewed differently following the 2001 scandal), we focused on events from 2014 and 2015 (these were the most recent years with complete CAR data at the time our research). Also, focusing on a specific time period reduced the number of economy- and industry-wide changes, which may impact CAR. To select cases, we used a comprehensive sampling strategy that minimized the risk of selection bias. First, RAs searched through every article published in the *New York Times* (NYTs; $N = 71,063$) and *Wall Street Journal* (WSJ; $N = 201,429$) in 2014 and 2015, which are the most influential newspapers dealing with business issues (Gunthorpe 1997). RAs were instructed to flag any articles that appeared to reflect “organizational actions that are deemed immoral or unacceptable according to societal norms or general standards of conduct” (Pfarrer et al. 2008, p. 731). RAs were instructed to take a liberal approach and include any story that seemed even tangentially relevant. We also reviewed every SEC press release and all red flagged events in the Capital IQ Key Events database to verify that the NYTs or WSJ covered all the relevant events.

Once all relevant articles were compiled, we conducted several steps to determine if they should be included in our sample. First, one assumption of the event study methodology and our theory is that an event provides new information to the market. Thus, we focused on news stories that reported on organizational unethical behaviors for the first time. We checked if the story was the first time the event was reported on by searching through all of ProQuest and Factiva, and conducting extensive general Internet searches. Second, another assumption of the event study methodology is that the researcher has isolated the effect of a focal event from the effects of other events. Thus, once

UNETHICAL BEHAVIOR IN CONTEXT

we located the first date that the news story was reported on, we searched for confounding stories occurring within the focal firm during the event window. For example, we made sure that no news stories about mergers and acquisition, CEO retirement, etc., occurred the day before or the day after the news story. If there were confounding events, the story was not included. Based on those criteria, our sample consisted of 158 independent events, covering 96 S&P 1500 firms, and 37 industries.

Independent variables: Article coding

Coders. Our article coding process involved two attempts. First, to code the articles from 2014, we recruited two senior finance majors from a large university on the East Coast of the U.S. The coders, who were unaware of our predictions, were presented with the coding scheme and instructed to review each article from the perspective of an investor and anticipate how external stakeholders would react to the story. The logic was that investors may be personally agnostic regarding the morality of an unethical act, but they likely anticipate how the public will react. Coders evaluated the first 24 articles together, to confirm agreement, and then coded articles separately. Later, to increase our sample size, we added a second year (i.e., 2015). For this coding, we recruited two psychology students (one undergraduate and one graduate), and they both coded all articles for 2015. Coders exhibited sufficient levels of inter-rater reliability, which ranged from moderate to strong (ICC_1 ranged from .22 to .90, ICC_2 from .36 to .95; $F_{113,227} = 1.57$ to 18.68, all $ps < .05$; see Online Appendix Table 10 for full results), justifying aggregation to the event-level. All the analyses reported below led to the same conclusion when we use data from either year separately or both years combined, and hold with or without controlling for data collection period.

Measures

All items were measured on a 7-point scale (1 = “strongly disagree”; 7 = “strongly agree”).

Pro-organizational unethical behavior. We operationalized the beneficiary of the unethical behavior (i.e., an organization versus an individual) by asking the coders to rate if the act described in the story was intended to benefit: 1) an isolated individual or individuals personally, 2) the individual who engaged in the unethical act, 3) the focal organization as a whole, and 4) the company where the event occurred. The first two items represent the pro-self unethical behavior measure and the last two items represent the pro-organizational unethical behavior measure. While it is possible that some

UNETHICAL BEHAVIOR IN CONTEXT

unethical acts benefit both the firm and the actor, the two measures were strongly inversely correlated ($r = -.80$), suggesting that people tended to classify a given unethical act as either benefiting the actor or the firm. In addition, a confirmatory factor analysis of the four items revealed that a one-factor model fit the data significantly better than a two-factor model ($\Delta\chi^2_{1,157} = 192.88, p < .001$). We thus reverse-coded the first measure and averaged the two measures. Lower scores indicate that the unethical act was perceived as more pro-self and higher scores as more pro-organizational.

Morality of the organization's goals. We operationalized the morality of organizational goals by asking the coders to code how strongly they agreed or disagreed that: 1) the goal of the focal organization is a moral one, 2) the work that the focal organization does has a positive social impact, and 3) the work that the focal organization does impacts people's lives in a positive way.

Moral judgments of the unethical behavior. We operationalized moral judgments of the act by asking the RAs to code how strongly they agreed or disagreed that the act was: 1) wrong, 2) immoral, and 3) unethical. Higher values indicate an act being evaluated as more immoral.

Event-related stock market reactions. We used Eventus to estimate abnormal returns following each of the 158 events using the market-adjusted model based on an equally weighted index. Consistent with prior work, we used a window of -254 to -21 days prior to the event as the baseline period that an "abnormal return" is compared against (Palmrose et al. 2004). Following methodological recommendations for event studies (MacKinlay 2007, McWilliams and Siegel 1997), we used the time window of three (-1, 0, +1) trading days, where 0 is the date of the published story, -1 is the day before the story, and +1 is the day after. Previous research has shown that a three-day window is appropriate for measuring unexpected events, such as news about unethical acts, as it allows for information leakage as well as potentially slower responses (Zhang and Wiersema 2009). To evaluate the appropriateness of the -1,+1 window, we examined Patell z values. As shown in Online Appendix Table 1, Patell z values were only significant for this window, and not alternative simulated windows, which suggests a -1,+1 window is where observed returns differed significantly.

Controls. We controlled for firm reputation with measures of market capitalization and firm sales (Godfrey et al. 2009) and whether the firm was listed on the Fortune 100 Best Companies list (Griffin and Mahon 1997) in the focal year (0 = No, 1 = Yes). Coders also coded for perceived

familiarity (two items: “I was familiar with the focal organization prior to reading this story,” and, “I had heard of the focal organization prior to reading the story”) and reputation (two items: “The focal organization has a very good reputation,” and, “The focal organization is respected by the general public”) of the focal firm. To examine whether effects persisted after controlling for CSR activity, we controlled for a proxy of CSR by compiling data from the Kinder, Lydenberg, and Domini (KLD) index, a source of data on companies’ social responsibility (Griffin and Mahon 1997); we separately summed the total number of listed strengths and concerns, which included performance in such categories as employee relations, diversity, human rights, and products. To account for the role of firm performance, which may have an effect on investors’ valuations (Hirshleifer and Teoh 2003), we extracted information on return on assets (ROA) and earnings before interest, taxes, depreciation and amortization (EBITDA). Since signals of distress can impact stock valuation, we also controlled for expected growth, measured by market-to-book-value (MTBV) (Fama and French 1992).

It is possible that pro-self and pro-organizational unethical behaviors could systematically differ in terms of 1) the magnitude of the act (e.g., with pro-self acts being smaller in magnitude, such as employee theft, and pro-organizational acts being larger, such as embezzling) and 2) expected legal sanctions (e.g., pro-self acts, such as employee theft, may be less likely to trigger legal fines). Thus, we controlled for both the magnitude of the act, using two items from McMahon and Harvey (2006) scale of perceived moral intensity, and the likelihood that an event would trigger a fine or legal action by having coders code for both constructs³. At the same time, while these controls address the possibility that different unethical acts might not be comparable along important dimensions (an effect that we do not empirically find; see Online Appendix), it is possible that these constructs partially control for the very process we theorize about. Thus, we note that our results hold with and without controls, and they also hold with all controls but magnitude and likelihood of a fine.

Analytical approach

Though all of our events were independent (i.e., we only coded the first newspaper story of an event), several organizations were in our sample of events more than once. For example, Wal-Mart

³ We acknowledge that it is possible that even with the training provided, the coders may have been unqualified to assess the likelihood that an unethical act would trigger a fine or the magnitude of the act.

UNETHICAL BEHAVIOR IN CONTEXT

was in our sample six times for six separate events. To account for possible non-independence among cases occurring in the same firm, in all analyses we used cluster-robust standard errors with events clustered within firms (Wooldridge 2003). For all analyses, we standardized all measures (to ease interpretation of the interactions). We used the following regression equations to test our hypotheses:

$$[1] \text{Moral judgments}_{ij} = \beta_0 + \beta_1 X + \beta_2 Z + \beta_3 XZ$$

$$[2] \text{CAR}_{ij} = \beta_{10} + \beta_{11} X + \beta_{12} M + \beta_{13} MX$$

$$[3] \text{CAR}_{ij} = \beta_{10} + \beta_{11} + \beta_{12} (\beta_0 + \beta_1 X + \beta_2 Z + \beta_3 XZ) + B_{13} (\beta_0 + \beta_1 X + \beta_2 Z + \beta_3 XZ) X$$

For equation 1, $\text{moral judgment}_{ij}$ is the predicted mean of moral judgment (for firm i and focal event j), $\beta_1 X$ is pro-organizational unethical behavior, $\beta_2 Z$ is perceived morality of the organization's goals, $\beta_3 XZ$ is the first stage interaction. Equation 1 tests the first-stage moderator hypothesis. For equation 2, CAR_{ij} is the cumulative abnormal return (for firm i for the two days surrounding the focal event j), $\beta_{11} X$ is moral judgment of the act, $\beta_{12} M$ is pro-organizational unethical behavior, $\beta_{13} MX$ is the second stage interaction. Equation 2 tests the second-stage moderator hypothesis. Once equation 3 is decomposed, the simple slopes can be computed at four levels – Low Z (low morality of goals), High Z (high morality of goals), Low X (low pro-organizational unethical acts), and High X (high pro-organizational unethical acts). In Study 2, CAR is replaced with estimated stock performance.

Results

Table 1 provides Study 1 variable summaries, reliabilities, and correlations. Table 2 reports the results of the hypotheses tests.

[Insert Tables 1 and 2 approximately here]

Moral judgments of unethical behaviors. Hypothesis 1 predicts that pro-organizational unethical behaviors are judged less harshly within organizations that are perceived as having a more moral goal. As displayed in Table 2, Model 3a, the interaction between pro-organizational unethical behavior and perceived morality of the organizational goal was significant ($b = -.11, p = .04$). See Figure 2 for a visual depiction of the interaction. When the morality of the organization's goals was rated at one standard deviation above the mean, the more the unethical act was seen as pro-organizational the less harshly it was judged ($b = -.42, p < .001$). As the morality of the organization's

UNETHICAL BEHAVIOR IN CONTEXT

goals decreased, the effect weakened, and at one standard deviation below the mean it was markedly weaker ($b = -.21, p < .001$), reaching non-significance at the lowest point of the morality of the organization's goals ($b = -.11, p = .08$). These results support Hypothesis 1.

[Insert Figure 2 approximately here]

Stock performance. Hypothesis 2 predicts that there will be more negative stock market reactions in response to harsher moral judgments of the act when the unethical behavior was perceived as benefiting the organization versus the actor. As displayed in Table 2, Model 3b, the interaction between moral judgments and pro-organizational unethical behavior was significant, ($b = -.30, p = .02$). See Figure 3 for a visual depiction of the interaction. When unethical acts were rated at one standard deviation above the mean in terms of benefiting the firm versus an individual, moral judgments of the act related strongly and negatively to CAR ($b = -.38, p < .001$). As the perceived beneficiary became more pro-self, the effect weakened, and at one standard deviation below the mean it was non-significant ($b = .22, p = .30$). These results support Hypothesis 2.

[Insert Figure 3 approximately here]

Moderated mediation test. Our full model implies that pro-organizational unethical behavior will have an indirect effect on stock prices, mediated through moral judgments of the act, and the effect will be stronger in the first stage when the morality of the organizational goal is high and in the second stage when the unethical behavior is pro-organizational. We tested this model by computing bias-corrected confidence intervals (with 5,000 bootstraps) of the product of the two paths. The models for each stage were estimated in the same way as those reported for Hypotheses 1 and 2, and structural equation modeling was used to combine the two paths. Per methodological recommendations for structural equation modeling (Kline 2011; p. 23), in mediation tests based on structural equation modeling we report unstandardized estimates with their confidence intervals, corresponding standard errors, and standardized estimates. Perception that the unethical behavior was more pro-organizational relative to more pro-self had a significant indirect effect, mediated through moral judgments, but only when the organization's goal was seen as more moral (first stage moderation), and only at high ($b = .23, SE = .10, CI [.09, .47], B = .16$) but not low ($b = .00, SE = .10, CI [-.20, .13], B = .12$) levels of the unethical behavior being seen as pro-organizational (second stage

moderation). Perception that the unethical act was more pro-organizational relative to more pro-self had no indirect effect when the organization goal was seen as less moral (first stage moderation), whether at high ($b = -.13$, $SE = .15$, $CI [-.51, .07]$, $B = -.09$) or low ($b = .00$, $SE = .06$, $CI [-.07, .22]$, $B = -.07$) levels of the unethical behavior being seen as pro-organizational (second stage moderation). Thus, pro-organizational unethical behavior has a positive effect on CAR compared to pro-self unethical behavior through moral judgments, but only when occurring within a firm with more (but not less) moral goals, and only at sufficiently high (but not low) levels of the unethical behavior being seen as pro-organizational. For example, on August 20, 2014, the New York Times printed an article about how Berkshire Hathaway (an organization that was rated as having high moral goals) was being investigated for anti-trust activities (an act that was rated as high on pro-organizational unethical behavior). However, Berkshire Hathaway saw a positive CAR of .39% following the story.

Robustness checks. We conducted several robustness checks to assess the strength of our findings. We reran all the analyses both with and without controls and we found the same pattern of direction and significance of the effects irrespective of the inclusion of controls (Online Appendix Table 9). Second, to account for possible non-independence among data coming from firms as well as different industry sectors, we tested the hypotheses using a three-level model with cases nested within firms and industry, and this analysis led to substantively the same results (Online Appendix Tables 6 and 7). Third, following advice by MacKinlay (2007), we simulated counterfactual results using different event dates. We created 10 new CAR measures using randomly generated dates and then reran these 10 models. All of the interaction terms testing our hypotheses for these alternative models (i.e., models predicting abnormal returns on random dates) were non-significant, with p -values ranging from .12 to .98. Thus, our model predicts CAR following unethical organizational behaviors, but not on random dates, suggesting that the pattern of results is specific to unethical acts rather than reflecting unrelated stock price fluctuations (Online Appendix 2, 3a, and 3b). The “Exploratory analysis” section of the online appendix elaborates on different specifications of our model and discusses main effect findings not explicitly explored through our hypotheses.

Study 1 discussion

In terms of substantive importance of the effects observed in Study 1, as shown in Table 2

(Model 2a and 3a), the main effects of pro-organizational unethical behavior and the morality of the organization's goals, and the interaction term for these constructs, accounted for 10 percent of variance in moral judgments ($\Delta R^2 = .10, p < .05$). This is comparable to other studies that have looked at moral judgments as an outcome (cf. $R^2 = .10, p < .05$ in Derfler-Rozin et al. 2018, Study 1; partial $\eta^2 = .13, p < .05$ in Leach et al. 2007, Study 2). As shown in Table 2 (Model 2a and 3a), the main effects of moral judgments and pro-organizational unethical behavior, and the interaction between these constructs, accounted for 7 percent of variance in CAR ($\Delta R^2 = .07, p < .05$), which is comparable to other studies that have examined CAR following news of unethical behavior (cf. $\Delta R^2 = .04, p < .05$ in Godfrey et al. 2009).

Study 2: Experiment

In Study 2, we sought to strengthen the internal validity of our conclusions through an experiment. One important assumption of Study 1 was that investors anticipate how the public is going to react, which we assume drives changes in stock performance. Study 2 allowed us to capture reactions by the public in a more representative manner because we recruited a sample that is demographically similar to the general population and we measured their moral judgments and their estimation of stock price changes following a news story of unethical behavior. Anticipated reaction is a good proxy for actual reactions since stock valuation fluctuate based on anticipated reactions by external stakeholders and the general public (Higgins and Reimers 1995). We wanted to ensure that the scenarios had experimental realism and that participants had "skin in the game," so participants were given an opportunity to earn money based on the accuracy of their stock price performance estimates. If the stock decreased by 3% and they estimated a 3% decrease, they were 100% accurate and received the maximum bonus. However, if they estimated a 2% decrease, they were only partially correct and were compensated depending on the extent to which they were accurate. This operationalization mirrors what happens in reality, since investors are rewarded for accurate predictions in stock performance. Finally, Study 2 also operationalized the dependent variable in a similar way as in Study 1. In Study 1 we looked at CAR, which is the difference between the expected return and the actual return of a stock, and in Study 2 we calculated the difference between how the

stock was expected to perform and how it actually performed.⁴

Method

Participants. We used Amazon's MTurk to recruit individuals who are demographically similar to the general population (Buhrmester et al. 2011). We recruited 230 participants: 64.5% were male, the average age was 34.5 ($SD = 10.75$), and 72 percent were White. All participants were from the U.S. The sample size was determined in advance and there were no exclusions of cases.

Design. Participants were randomly assigned to each of the four conditions of a 2 (unethical behavior beneficiary: pro-self vs. pro-organization) \times 2 (morality of the organization's goal: low vs. high) within-subject design. Participants read actual newspaper stories reporting on organizational unethical behavior and then responded to the measures.

Manipulation. We selected real newspaper articles that were as symmetric as possible across the different conditions. For example, in both pro-self conditions, participants read about employee theft. In both pro-organizational conditions, participants read about the focal firm overcharging customers. In both low morality conditions, participants read about an oil company (Exxon). In both high morality conditions, participants read about a supermarket featuring organic foods (Whole Foods). The actual name of the focal firm was scrubbed from the article and replaced with a short firm biography (taken from Capital IQ). The logic for this was to isolate the effect of the goals of the firm and reduce noise as a result of personal beliefs that individuals might have about the specific firms.

Measures

All items were measured on a 7-point scale (1 = "strongly disagree"; 7 = "strongly agree").

Pro-organizational unethical behavior (manipulation check). Participants were asked to rate how strongly they agreed or disagreed that the act described was intended to benefit: 1) an isolated individual or individuals personally, 2) the individual who engaged in the unethical act, 3) the focal organization as a whole, and 4) the company where the event occurred. The first two items represent the pro-self unethical behavior measure whereas the last two items represent the pro-organizational unethical behavior measure. As in Study 1, the measures were inversely correlated, $r = -.84$, $p < .001$,

⁴ We also conducted a between-subject experiment not reported here, which used standardized scenarios instead of real articles to address potential issues with idiosyncratic content; we found the same pattern of results. The full write-up of these findings and all data are available through the Open Science Framework link noted above.

UNETHICAL BEHAVIOR IN CONTEXT

and a one-factor model fit the data better than a two-factor model ($\Delta\chi^2_{1, 919} = 478.22, p < .001$). We thus reverse-coded the first measure and averaged the two measures.

Perceived morality of the organization's goals (manipulation check). Participants were asked to rate how strongly they agreed or disagreed that: 1) the goal of the focal organization is a moral one, 2) the work that the focal organization does has a positive social impact, and 3) the work that the focal organization does impacts people's lives in a positive way.

Moral judgments of the unethical behavior. Participants were asked to rate how strongly they agreed or disagreed that the act was: 1) wrong, 2) immoral, and 3) unethical.

Estimating stock performance. We asked participants to anticipate what they thought the closing value of the stock for the focal firm would be the day after the newspaper story was published. We asked them to predict the percentage gain or loss in the value of the stock compared to the expected value had the news story never been published (i.e., if they thought the stock would decrease 5% the day after the story was published, compared to the expected value, they would select "-5%"). To make sure our measure was consistent with the CAR measure, we provided participants with the actual *expected* return for the focal company the day after each story was published, asking them to anticipate the relative return, i.e., the extent to which the return would deviate (positively or negatively) in response to the event, relative to the return that would be expected if the event did not occur. The measure ranged from -10% to +10%.

Analytical approach

Since this was a within-person study, we used within-individuals cluster-robust standard errors (Wooldridge 2003). We used the continuous measures for perceived pro-organizational unethical behavior and morality of the organization's goals. We find an equivalent pattern of results when we estimate the model using the binary measures representing the experimental conditions. We report the full results of the analysis using the binary measures in Online Appendix Table 11. We used continuous measures in the main analyses because we wanted to allow people's perceptions of the constructs to vary as they do in reality, continuously, making this operational definition aligned with our conceptual focus. This approach also allowed us to test the process in a way that mirrors Study 1 and interpret the moderated mediation model in a meaningful manner.

Results

Table 3 provides Study 2 variable summaries, reliabilities, and correlations.

[Insert Table 3 approximately here]

Stimuli assessment. To check that the stimuli (i.e., newspaper stories) elicited the expected perceptions in the appropriate category, we conducted a 2 (unethical behavior beneficiary) \times 2 (morality of the organizational goals) multivariate regression. Stories in the pro-organizational condition were perceived as benefiting the organization more ($M = 5.79$, $SD = 1.19$) than stories in the pro-self condition ($M = 1.69$, $SD = 1.01$), $b = .19$, $p < .001$. Additionally, stories in the low morality condition were perceived as having organizations with less moral goals ($M = 2.66$, $SD = 1.40$) than stories with organizations in the high morality condition ($M = 5.18$, $SD = 1.46$), $b = .17$, $p < .001$. In addition, there was no contamination between the two factors (p 's for all interactions $> .05$). Thus, the manipulations were effective and orthogonal to each other.

Moral judgments of unethical behaviors. As displayed in Table 4, Model 2a, the interaction between pro-organizational unethical behavior and perceived morality was significant ($b = -.11$, $p < .001$). Figure 4 depicts the interaction. When the morality of the organization's goals was rated at one standard deviation above the mean, pro-organizational unethical behavior was judged less harshly than pro-self unethical behavior ($b = -.21$, $p < .001$). As the morality of the organization's goals decreased, the effect reduced, and at one standard deviation below the mean it was non-significant ($b = .02$, $p = .66$). These results support Hypothesis 1.

[Insert Figure 4 approximately here]

Stock price estimation. As displayed in Table 4, Model 2b, the interaction between judgments of the unethical behavior and unethical behavior beneficiary was significant, ($b = -.07$, $p = .03$). See Figure 5 for a visual depiction of the interaction. When unethical behaviors were rated at one standard deviation above the mean in terms of benefiting the organization rather than the individual, judgments of the unethical act related more strongly and negatively to estimated stock performance ($b = -.23$, $p < .001$). As the perceived beneficiary became more pro-self, the effect reduced; at one standard deviation below the mean it was markedly weakened ($b = -.09$, $p = .04$), reaching non-significance at the lowest point on the scale of the extent to which the unethical act was perceived to be pro-

organizational rather than pro-self ($b = -.17, p = .11$). These results support Hypothesis 2.

[Insert Table 4 and Figure 5 approximately here]

Moderated mediation test. The same moderated mediation analysis approach was used as in Study 1. Perception that the unethical behavior was more pro-organizational had a significant indirect effect, mediated through moral judgments, but only when the organization's goal was seen as more moral (first stage moderation), and only at high ($b = .07, SE = .02, CI [.04, .11], B = .04$) but not low ($b = -.01, SE = .02, CI [-.04, .02], B = .00$) levels of the unethical behavior being seen as pro-organizational (second stage moderation). Perception that unethical behavior was more pro-organizational had no indirect effect when the organization's goal was seen as less moral (first stage moderation), whether at high ($b = .03, SE = .03, CI [.00, .09], B = .02$) or low ($b = .00, SE = .01, CI [-.02, .01], B = .00$) levels of the unethical behavior being seen as pro-organizational (second stage moderation). Thus, consistent with the results of Study 1, pro-organizational compared to pro-self unethical behavior has a positive effect on estimated stock prices through moral judgments, but only when occurring within an organization with more (but not less) moral goals, and only at sufficiently high (but not low) levels of the unethical behavior being seen as pro-organizational.

Study 2 discussion

Study 2 allowed us strengthen the internal validity of our conclusions and assess if the public reacted in a way that conformed to our theory. In terms of importance of the effects observed, the main effects of pro-organizational unethical behavior and the morality of the organization's goals, and the interaction term for these constructs, accounted for 3 percent of variance in moral judgments ($R^2 = .03, p < .05$). Though this effect was smaller than the effect found in the field (Study 1), the second stage of our model accounted for 30 percent of variance in stock estimation ($R^2 = .30, p < .05$).

General discussion

News stories about organizational unethical acts appear frequently, and the resulting stock market responses can have a profound influence on the firms involved. Our model contributes to the ability to understand and predict such consequential outcomes of organizational unethical acts. Relying on work in moral psychology, we proposed that the more moral the goal of the organization is perceived to be, observers judge pro-organizational unethical acts more leniently than pro-self

UNETHICAL BEHAVIOR IN CONTEXT

unethical acts. Moral judgments of the unethical act in turn translate into negative stock performance for the firm primarily when the unethical act is pro-organizational, but less so when the act is pro-self. Two studies found evidence consistent with our model. Study 1 was an event study of stock market reactions to organizational unethical acts. Study 2 was an experiment where we manipulated the features of unethical acts and the firm context and measured predictions of stock performance.

Theoretical Implications. Our paper advances prior work on stock market reactions to organizational unethical behavior. Considering nuances of both the unethical act, and the firm context where the act occurs, allowed us to move beyond extant models and generate new predictions. Most notably, even though the property of an unethical behavior being pro-organizational, compared to pro-self, can attenuate moral judgments of the act, at least in the context of a firm that is perceived to have a more moral goal, the same property can amplify negative economically-relevant outcomes for the firm (reflected in stock performance) resulting from moral judgments of the act. This finding adds substantial precision in predicting stock market reactions to organizational unethical behavior.

Our studies also suggest that a firm-level factor that can be considered constructive (i.e., being perceived as an organization with moral goals) can temper judgments of pro-organizational unethical acts. Prior CSR research has made similar arguments, noting that pro-social programs can create moral capital for a firm, which acts as “insurance-like” protection in the event of unethical organizational acts becoming known (Flammer 2013, 2015, Godfrey et al. 2009, Pelozo 2006). We advance this work in two ways. First, we demonstrate the utility of a conceptually more general category that might drive the buffering effects—the perceived morality of the organization’s goals. Though this construct may emerge as a result of CSR programs, we show that the mere perception that a firm has moral goals (even absent CSR programs) can produce buffering effects. This is important because arguably all firms, irrespective of their CSR programs, vary in the extent to which their primary goals are perceived as moral. Thus, our theorizing broadens the scope of explanations linking moral capital generated by organizational activities with reactions to organizational unethical behavior. Second, we show that irrespective of the perception of organizational investment in morally commendable activities, organizations can suffer in terms of stock performance, determined by anticipated public reaction, if the act is seen as benefiting the firm. Thus, we demonstrate the

UNETHICAL BEHAVIOR IN CONTEXT

importance of taking into account not just firm-level activities, but also the individual actor who committed the unethical behavior (and specifically his or her intended beneficiary), revealing conditions where this “insurance-like” protection may have less of an added value.

Third, our work has implications for research that looks at personal versus social motives for unethical behavior in organizations (Thau et al. 2015, Umphress et al. 2010). The psychological work in this area has focused primarily on the antecedents to these behaviors. It has been important in explaining when and why individuals engage in these behaviors and informing ways of eliminating these acts, but it says little about when and why pro-organizational unethical acts do or do not translate into economically-relevant outcomes for the firm. On the other hand, firm-level research in strategy, finance, and economics has looked at the outcomes of unethical acts, but did not distinguish between pro-organizational and pro-self unethical acts (e.g., Baucus and Near 1991, Bennett et al. 2013, Zitzewitz 2012). We contribute to the literature by integrating these two perspectives and showing that pro-self versus pro-other unethical behaviors elicit different responses and ultimately lead to different outcomes for the firm depending on the features of the organizational context.

Managerial implications. Our theory has implications for managers and policy makers. Employees have been shown to engage in pro-organizational unethical acts because they want to help the firm (Umphress et al. 2010). However, our findings suggest that in certain cases such acts cause severe damage and should be especially discouraged—despite the “good intentions” underlying the act. For example, in 2015, Wells Fargo was hit with a \$185 million fine for employees engaging in illegal sales practices that included opening credit-card accounts without customers' knowledge, acts that clearly benefited the bank. Managers might explain that it is these kinds of acts that have the potential to hurt the organization the most. By clearly communicating this fact, managers might undercut the motivation of employees to “help” the organization by crossing ethical boundaries.

Second, our research has policy implications. Instances of the unethical behavior benefiting firms with moral goals might go unnoticed, as the first link in our model might be “broken” and such ethical violations will be less likely to be judged as immoral. Thus, within organizations pursuing a more moral goal, what may be considered “minor” unethical violations might go unnoticed. This may make managers more complacent when reacting to unethical acts in firms with moral goals. It may

UNETHICAL BEHAVIOR IN CONTEXT

also make managers and the public less likely to be sensitive to degradation in ethical conduct of firms with moral goals, in line with the “slippery slope effect,” showing that people are less likely to criticize the conduct of others when behaviors erode gradually as opposed to abruptly (e.g., Gino and Bazerman 2009). Thus, a greater scrutiny of organizations with moral goals may be warranted.

Limitations and future directions. Reactions to unethical acts that occur within firms are a multi-determined phenomenon and reactions are driven by multiple factors. Our theory focuses on one specific response (related to stock prices) of a general group (the public), and we also only focus on moral judgments as an explanatory mechanism. Concerns about the health of the firm or its ability to maintain adequate functioning may also impact other outcomes (e.g., buy-and-hold strategies, valuations, etc.). While we did not focus on such considerations, or other outcomes, the process we describe should drive negative reactions irrespective of other factors. Across cultures, people make judgments of unethical acts and exhibit negative reactions even when it is costly (Henrich et al. 2006). We also believe that the pattern of effects proposed by our theory cannot be explained by confidence in firm functioning. For instance, in some cases (e.g., firms with moral goals), pro-organizational unethical behavior is judged less harshly. Yet, it is not clear if pro-organizational unethical behavior would lead to a greater confidence in the health of the firm than pro-self acts. Future research is needed to explore the interplay between moral judgments of organizational unethical acts and other relevant considerations, such as those about a firms’ ability to maintain adequate functioning, and also examine how our theory predicts other firm-relevant outcomes of unethical acts.

Furthermore, we do not look at either the consequences for the individual(s) engaging in these unethical acts, or the context of non-publically traded firms (e.g., charities, NGOs, etc.). However, our research does begin to highlight the importance of studying unethical acts in the context of organizations with highly moral goals. Since the scandals at Enron, WorldCom, and Adelphia, these firms have become household names for unethical behavior. Less discussed are similar acts within humanitarian organizations such as Oxfam, AED, or Red Cross. Thus, an area for future research is the setting of more moral organizations, such as NGOs and charities, which might unintentionally encourage unethical behavior. Future studies could explore if pro-organizational unethical behavior is more likely to shift into pro-self unethical behavior within contexts of more moral organizations.

Conclusion. This paper shows that how the public perceives the beneficiary of the act, and the morality of the organization's goals, determines economic consequences of organizational unethical behaviors for the firm. Our theory embraces a fundamental, but often overlooked, reality of these acts: though they are committed by individuals, they also occur within a specific firm context. Using a multi-method approach, we show that even though pro-organizational unethical behaviors are judged less harshly in moral organizations, that same type of act results in the firm likely being viewed as an "accomplice" and thus hurts stock performance as a result. These findings are important for understanding reactions to organizational unethical behavior and thus contribute to an integrated, contextualized understanding of consequences of unethical acts within organizations.

References

- Alicke M, Buckingham J, Zell E, Davis T (2008) Culpable control and counterfactual reasoning in the psychology of blame. *Person. and Social Psych. Bull.* 34(10):1371–1381.
- Alter A, Kernochan J, Darley (2007) Transgression wrongfulness outweighs its harmfulness as a determinant of sentence severity. *Law and Human Beh.* 31(4):319–335.
- Baucus M, Near J (1991) Can illegal corporate behavior be predicted? An event history analysis. *Acad. Management J.* 34(1):9–36.
- Bennett V, Pierce L, Snyder J, Toffel M, (2013) Customer-driven misconduct: How competition corrupts business practices. *Management Sci.* 59(8):1725–1742.
- Brady F (1985) A Janus-headed model of ethical theory: Looking two ways at business/society issues. *Acad. Management Rev.* 10(3):568–576.
- Buhrmester M, Kwang T, Gosling S (2011) Amazon's Mechanical Turk: A new source of inexpensive, yet high-quality, data? *Perspectives on Psych. Sci.* 6(1):3–5.
- Darley J (2009) Morality in the law: The psychological foundations of citizens' desires to punish transgressions. *Annual Review Law and Social Sci.* 5:1–23.
- Davidson W, Worrell D, Garrison S (1988) Effect of strike activity on firm value. *Acad. Management J.* 31(2):387–394.
- Derfler-Rozin R, Baker B, Gino F (2018) Compromised ethics in hiring processes? How referrers'

UNETHICAL BEHAVIOR IN CONTEXT

- power affects employees' reactions to referral practices. *Acad. Management J.* 61(2): 615–636.
- Eisenhardt K (1989) Agency theory: An assessment and review. *Acad. Management J.* 14(1):57–74.
- Fama E, French K (1992) The cross-section of expected stock returns. *J. Fin.* 47(2):427–465.
- Fehr E, Gächter S (2000) Fairness and retaliation. *J. Econ. Per.* 14(3):159–181.
- Flammer C (2013) Corporate social responsibility and shareholder reaction: The environmental awareness of investors. *Acad. Management J.* 56(3):758–781.
- Flammer C (2015) Does corporate social responsibility lead to superior financial performance? A regression discontinuity approach. *Management Sci.* 61(11):2549–2568.
- Fritzsche D, Becker H (1984) Linking management behavior to ethical philosophy: An empirical investigation. *Acad. Management J.* 27(1):166–175.
- Frooman J (1997) Socially irresponsible and illegal behavior and shareholder wealth. *Business & Society* 36(3):221–249.
- Gailey J, Lee M (2005) An integrated model of attribution of responsibility for wrongdoing in organizations. *Social Psych. Quart.* 68(4):338–358.
- Gino F, Bazerman M (2009) When misconduct goes unnoticed: The acceptability of gradual erosion in others' unethical behavior. *J. Exp. Social Psych.* 45(4):708–719.
- Gino F, Pierce L (2009) Dishonesty in the name of equity. *Psych Sci.* 20(9):1153–1160.
- Godfrey P, Merrill C, Hansen J (2009) The relationship between corporate social responsibility and shareholder value. *Strat. Management. J.* 30(4):425–445.
- Greve H, Palmer D, Pozner J (2010) Organizations gone wild: The causes, processes, and consequences of organizational misconduct. *Acad. Management Ann.* 4(1):53–107.
- Griffin J, Mahon J (1997) The corporate social performance and corporate financial performance debate: Twenty-five years of incomparable research. *Business & Society* 36(1):5–31.
- Gunthorpe D (1997) Business ethics: A quantitative analysis of the impact of unethical behavior by publicly traded corporations. *J. Business Ethics* 16(5):537–543.
- Haidt J, Kesebir S (2010) Morality. Fiske D, Gilbert J, Lindzey G, eds. *Handbook of Social Psychology* (5th ed) (Wiley, Hoboken), 797–832.

UNETHICAL BEHAVIOR IN CONTEXT

- Hamilton V (1986) Chains of command: Responsibility attribution in hierarchies. *J. App. Social Psych.* 16(2):118–138.
- Hamilton V, Sanders J (1995) Crimes of obedience and conformity in the workplace: Surveys of Americans, Russians, and Japanese. *J. Social Issues* 51(3):67–88.
- Hauser M (2006) *Moral Minds: How Nature Designed Our Universal Sense of Right and Wrong* (Ecco, New York).
- Henrich J, McElreath R, Barr A, Ensminger J, Barrett C, Bolyanatz A... Ziker J (2006) Costly punishment across human societies. *Science* 312(5781):1767–1770.
- Higgins R, Reimers M (1995) *Analysis for Financial Management*. (Irwin, Chicago).
- Hirshleifer D, Teoh S (2003) Limited attention, information disclosure, and financial reporting. *J. Account. and Econ.* 36(1):337–386.
- Jones T (1991) Ethical decision making by individuals in organizations: An issue-contingent model. *Acad. Management Rev.* 16(2):366–395.
- Jonsson S, Greve H, Fujiwara-Greve T (2009) The spread of legitimacy loss to innocent organizations in response to reported corporate deviance. *Admin. Sci. Quart.* 54(2):195–228.
- Karpoff J, Lee D, Vondra V (1999) Defense procurement fraud, penalties, and contractor influence. *J. Political Econ.* 107(4):809–842.
- King B, Soule S (2007) Social movements as extra-institutional entrepreneurs: The effect of protests on stock price returns. *Admin. Sci. Quart.* 52(3):413–442.
- Kline R (2011) *Principles and practice of structural equation modeling* (3rd ed). (Guilford, New York).
- Leach C, Ellemers N, Barreto M (2007) Group virtue: The importance of morality (vs. competence and sociability) in the positive evaluation of in-groups. *J. Person. and Social Psych.* 93(2):234–249.
- Lerner J, Goldberg J, Tetlock P (1998) Sober second thought: The effects of accountability, anger, and authoritarianism on attributions of responsibility. *Person. and Soc. Psych. Bull.* 24:563–574.
- Lindenmeier J, Schleier C, Pricl D (2012) Consumer outrage: Emotional reactions to unethical

UNETHICAL BEHAVIOR IN CONTEXT

- corporate behavior. *J. Business Research* 65(9):1364–1373.
- Lounsbury M, Hirsch P (2010) *Markets on Trial: The Economic Sociology of the U.S. Financial Crisis*. (Emerald, Bingley, UK).
- MacKinlay C (1997) Event studies in economics and finance. *J. Econ. Lit.* 35(1):13–39.
- Margolis J, Walsh J (2003) Misery loves companies: Rethinking social initiatives by business. *Admin. Sci. Quart.* 48(2):268–305.
- McMahon J, Harvey R (2006) An analysis of the factor structure of Jones' moral intensity construct. *J. Business Ethics* 64(4):381–404.
- McWilliams A, Siegel D (1997) Event studies in management research: Theoretical and empirical issues. *Acad. Management J.* 40(3):626–657.
- Mill JS (1897) *Utilitarianism* (Longmans, Green and Co., London).
- Miller K, Sturdivant F (1977) Consumer responses to socially questionable corporate behavior: An empirical test. *J. Consumer Res.* 4(1):1–7.
- Palmrose Z, Richardson V, Scholz S (2004) Determinants of market reactions to restatement announcements. *J. Account. and Econ.* 37(1):59–89.
- Paruchuri S, Misangyi V (2015) Investor perceptions of financial misconduct: The heterogeneous contamination of bystander firms. *Acad. Management J.* 58(1):169–194.
- Pelozo J (2006) Using corporate social responsibility as insurance for financial performance. *California Management Rev.* 48(2):52–72.
- Pfarrer M, Decelles K, Smith K, Taylor M (2008) After the fall: Reintegrating the corrupt organization. *Acad. Management Rev.* 33(3):730–749.
- Pinto J, Leana C, Pil F (2008) Corrupt organizations or organizations of corrupt individuals? *Acad. Management Rev.* 33(3):685–709.
- Rao S, Hamilton J (1996) The effect of published reports of unethical conduct on stock prices. *J. Business Ethics* 15(12):1321–1330.
- Rest J (1986) *Moral development: Advances in research and theory* (Praeger New York, NY).
- Simpson S (2002) *Corporate Crime, Law, and Social Control* (Cambridge University).

UNETHICAL BEHAVIOR IN CONTEXT

- Snyder J (2010) Gaming the liver transplant market. *J. Law, Econ., and Organ.* 26(3):546–568.
- Strachan J, Smith D, Beedles W (1983) The price reaction to (alleged) corporate crime. *Fin. Rev.* 18(2):121–132.
- Thau S, Derfler-Rozin R, Pitesa M, Mitchell M, Pillutla M (2015) Unethical for the sake of the group: Risk of social exclusion and pro-group unethical behavior. *J. Appl. Psych.* 100(1):98–113.
- Umphress E, Bingham J (2011) When employees do bad things for good reasons: Examining unethical pro-organizational behaviors. *Organ. Sci.* 22(3):621–640.
- Umphress E, Bingham J, Mitchell M (2010) Unethical behavior in the name of the company: The moderating effect of organizational identification and positive reciprocity beliefs on unethical pro-organizational behavior. *J. Appl. Psych.* 95(4):769–780.
- Wiltermuth S (2011) Cheating more when the spoils are split. *Organ. Behav. Hum. Dec.* 115(2):157–168.
- Wiltermuth S, Bennett V, Pierce L (2013) Doing as they would do: How the perceived ethical preferences of third-party beneficiaries impact ethical decision-making. *Organ. Behav. Hum. Dec.* 122(2):280–290.
- Wooldridge J (2003) Cluster-sample methods in applied econometrics. *Amer. Econ. Rev.* 93:133–138.
- Young L, Saxe R (2009) Innocent intentions: A correlation between forgiveness for accidental harm and neural activity. *Neuropsychologia* 47(10):2065–2072
- Zhang Y, Wiersema M (2009) Stock market reaction to CEO certification: The signaling role of CEO background. *Strat. Management J.* 30(7):693–710.
- Zitzewitz E (2012) Forensic economics. *J. Econ. Lit.* 50(3):731–769.

Figure 1 Theoretical Model

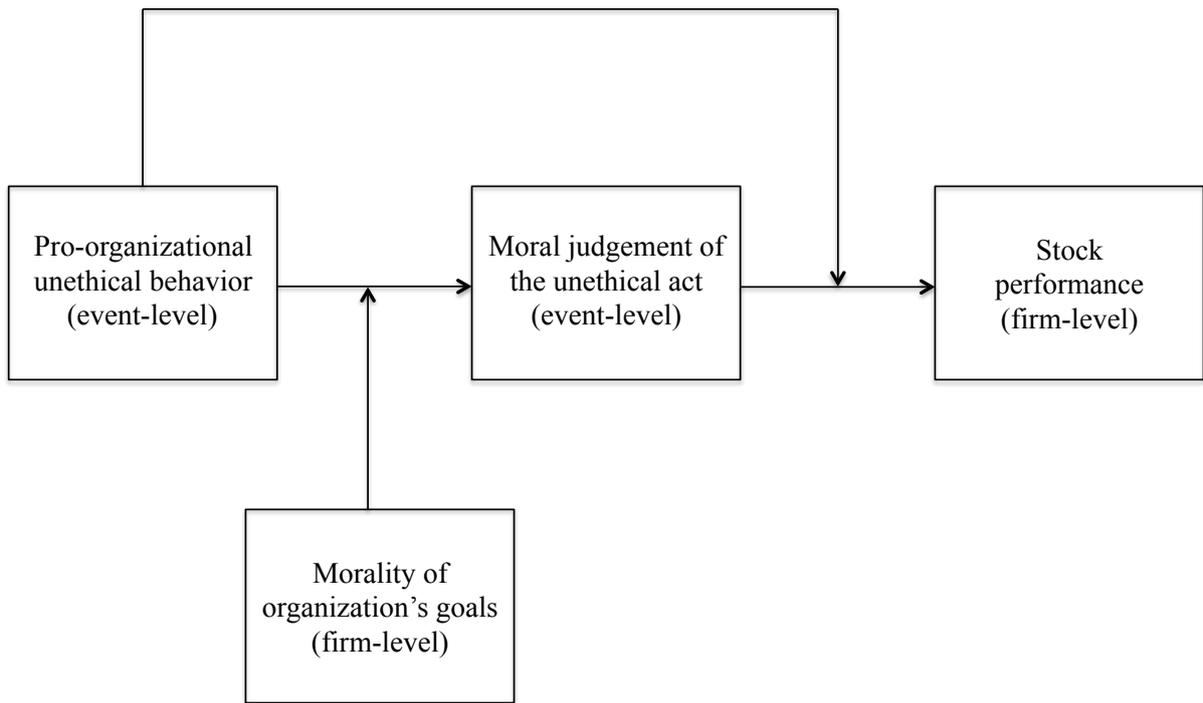
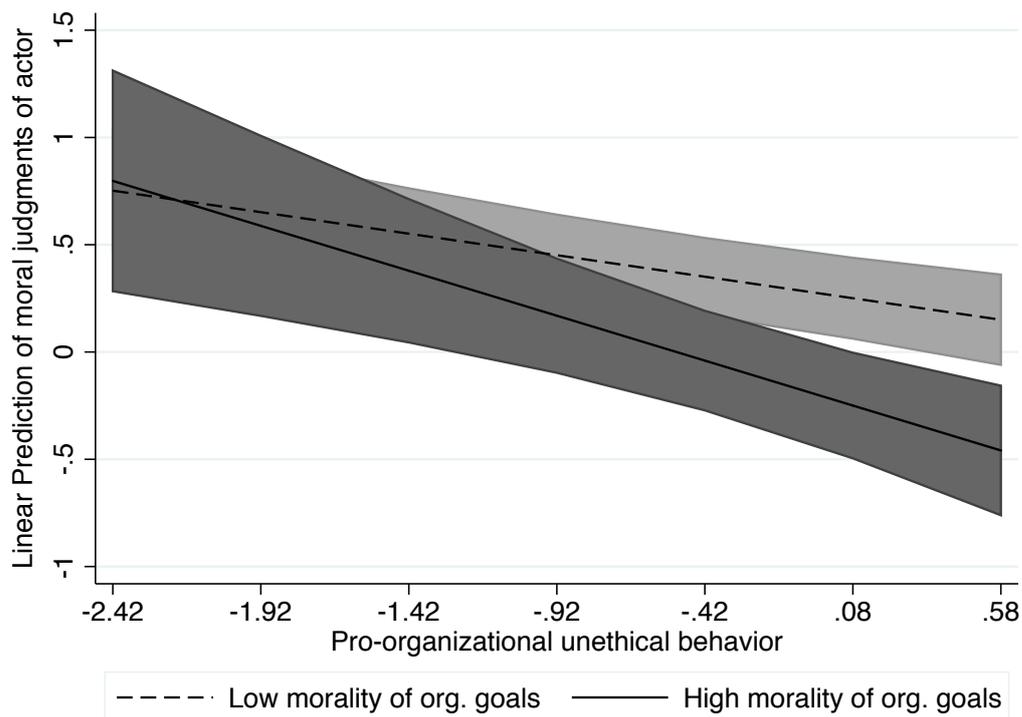
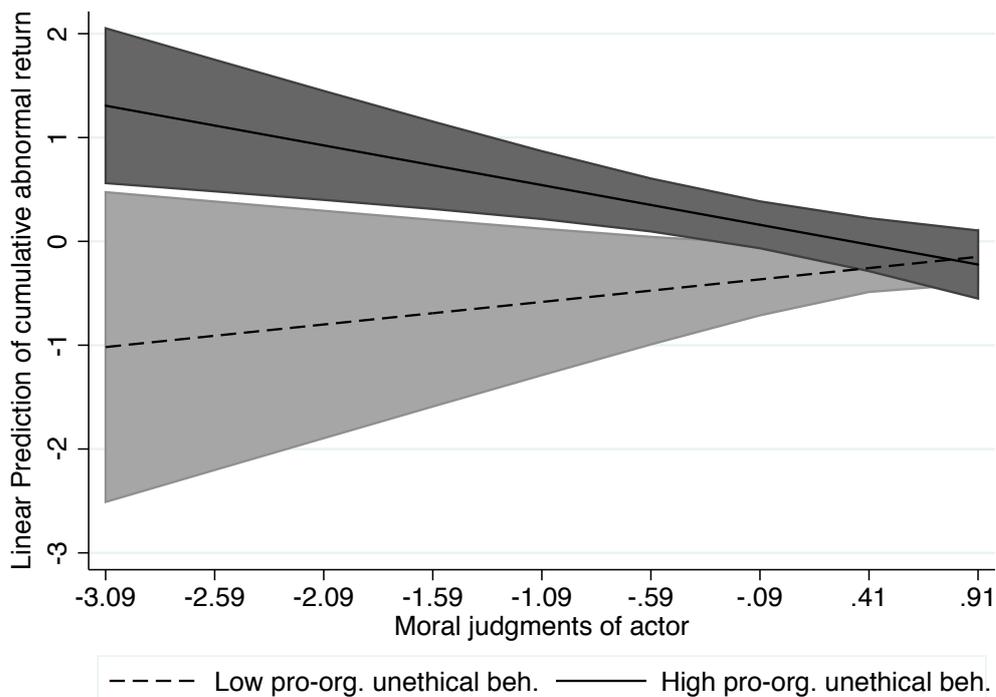


Figure 2 Moderating Effect of Organizational Goals on Moral Judgments (Study 1)



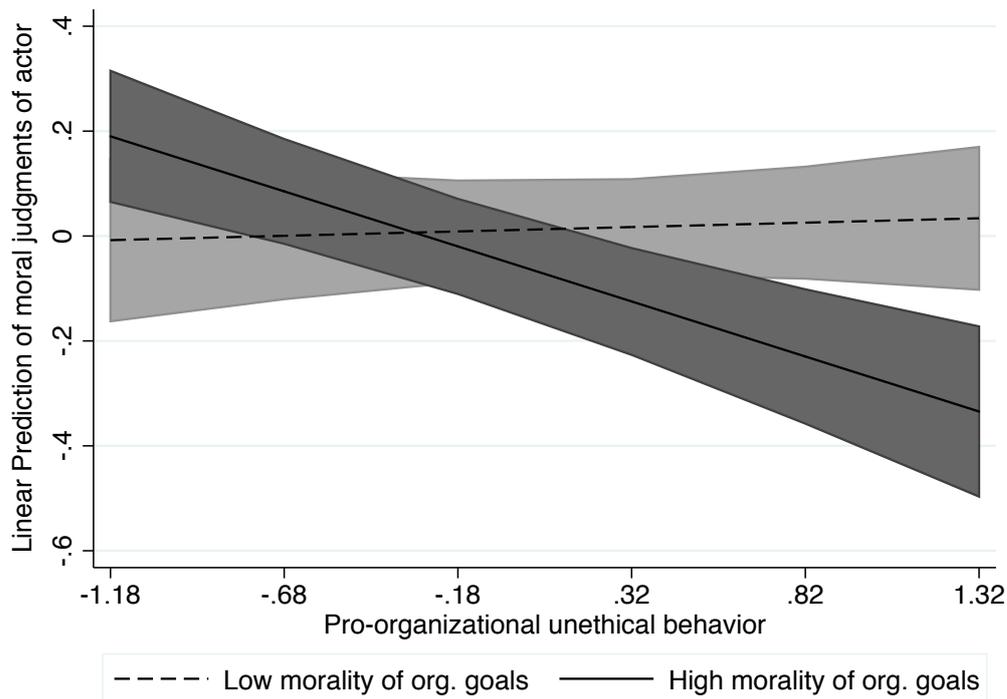
Note: Bands are 95% confidence intervals; higher values on the Y axis indicate an unethical act being judged as more immoral (standardized); the X axis shows the entire range of the standardized variable of the extent to which the unethical act is judged as pro-organizational (-2.42, 1.01); moderator set at +/- 1 SD.

Figure 3 Moderating Effect of Pro-Organizational Unethical Behavior on CAR (Study 1)



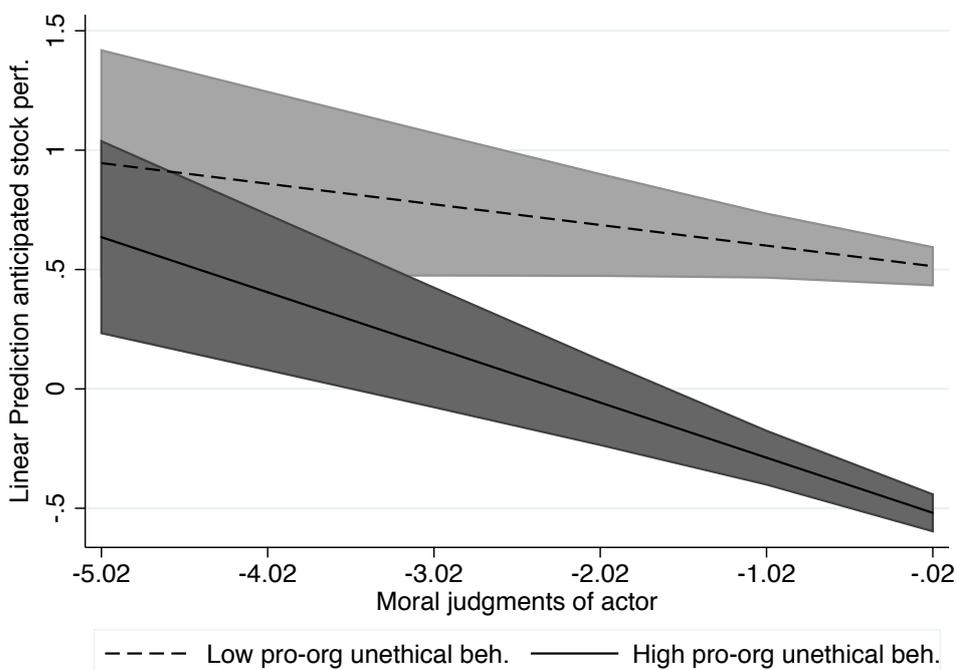
Note: Bands are 95% confidence intervals; X axis shows the entire range of the standardized variable of the extent to which the unethical act is judged as immoral (-3.09, 1.29); moderator set at +/- 1 SD.

Figure 4 Moderating Effect of Organizational Goals on Moral Judgments (Study 2)



Note: Bands are 95% confidence intervals. Higher values on the Y axis indicate an unethical act being judged as more immoral (standardized); the X axis shows the entire range of the standardized variable of the extent to which the unethical act is judged as pro-organizational (-1.18, 1.40); moderator set at +/- 1 SD.

Figure 5 Moderating Effect of Pro-Organizational Unethical Behavior on Anticipated Stock Performance (Study 2)



Note: Bands are 95% confidence intervals. X axis shows the entire range of the standardized variable of the extent to which the unethical act is judged as immoral (-5.02, .64); moderator set at +/- 1 SD.

Table 1 Study 1: Variable Means, Standard Deviations, Reliabilities, and Correlations (N = 158)

	M	SD	Min	Max	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	
1. Pro-org. unethical behavior ^a	5.23	1.75	1.00	7.00	(.95)																	
2. Morality of org. goals	4.37	1.52	1.83	7.00	.23	(.98)																
3. Moral judgments ^b	5.53	1.14	2.00	7.00	-.37	-.18	(.96)															
4. CAR (-1, 0, +1) ^c	-0.56	2.55	-10.92	6.74	.09	-.12	-.16	-														
5. Sales ^d	7.18	9.80	0.00	48.35	-.03	-.08	.08	.06	-													
6. Market cap. ^d	11.00	10.50	0.01	59.10	-.06	-.03	-.01	.16	.60	-												
7. KLD strengths	5.49	4.38	0.00	14.00	.02	-.03	-.04	.24	.35	.49	-											
8. KLD concerns	2.46	2.81	0.00	12.00	.03	-.01	.02	.14	.75	.57	.53	-										
9. Fortune listing	0.07	0.26	0.00	1.00	.13	.24	-.13	-.07	-.10	.03	.23	-.04	-									
10. ROA	0.04	0.06	-0.20	0.21	.18	.28	-.11	.12	.16	.35	.40	.30	.18	-								
11. EBIDTA ^d	1.75	1.73	-0.01	6.14	-.24	-.32	.15	.15	.57	.81	.41	.43	-.10	.08	-							
12. MTBV	0.01	0.05	-0.02	0.55	-.04	-.03	.00	-.37	-.09	-.14	-.15	-.11	-.03	-.09	-.13	-						
13. Familiarity	5.11	2.13	1.00	7.00	.06	.13	-.12	.14	.29	.39	.36	.35	.14	.22	.29	-.16	(.99)					
14. Reputation	4.78	1.09	2.00	7.00	.13	.42	-.24	.07	.02	.19	.19	.15	.16	.11	.00	-.13	.58	(.97)				
15. Coded fine	3.52	1.59	1.00	7.00	-.16	.03	.52	-.04	-.05	-.08	-.24	-.15	-.08	-.04	.04	.02	-.24	-.24	(.95)			
16. Magnitude	3.62	1.37	1.00	6.75	-.03	-.06	.34	-.02	-.03	-.08	-.10	-.13	-.01	.07	-.02	-.01	-.16	-.25	.28	(.96)		
17. Collection ^e	1.57	0.50	1.00	2.00	-.04	-.47	-.35	.20	-.07	.00	.02	-.09	-.06	-.14	.04	-.11	.11	.01	-.48	-.10	-	

Note: Cronbach's α values are in brackets on the diagonal. ^a Lower values indicate pro-self unethical behavior; higher values indicate pro-organizational unethical behavior. ^b Higher values indicate an act being evaluated as more immoral. ^c CAR displayed in percentage. ^d Mean and SD values are expressed in the ten thousands. ^e First round of event collections for 2014 = 1; second round of event collections for 2015 = 2. All correlations above $|\ .15|$ are significant at $p < .05$.

Table 2 Study 1: Regression Analyses of Moral Judgments & Cumulative Abnormal Returns

	Moral Judgments		Moral Judgments		Moral Judgments		Abnormal Returns		Abnormal Returns		Abnormal Returns	
	Model 1a		Model 2a		Model 3a		Model 1b		Model 2b		Model 3b	
	<i>b</i>	<i>SE</i>	<i>b</i>	<i>SE</i>	<i>b</i>	<i>SE</i>	<i>b</i>	<i>SE</i>	<i>b</i>	<i>SE</i>	<i>b</i>	<i>SE</i>
Sales	-0.06	0.11	-0.01	0.10	0.00	0.10	-0.15	0.09	-0.16	0.10	-0.10	0.10
Market capitalization	-0.17	0.16	-0.03	0.14	0.02	0.14	0.03	0.14	-0.02	0.14	-0.03	0.15
Forbes listed	-0.07	0.10	-0.04	0.09	-0.04	0.09	-0.13*	0.05	-0.15*	0.04	-0.15*	0.04
KLD strengths	0.09	0.09	0.06	0.09	0.06	0.09	0.20	0.09	0.22	0.10	0.24*	0.09
KLD concerns	0.12	0.14	0.07	0.13	0.03	0.13	0.11	0.13	0.13	0.13	0.10	0.13
ROA	-0.15	0.07	-0.08	0.08	-0.08	0.08	0.05	0.09	0.01	0.09	0.03	0.09
EBIDTA	0.22	0.12	-0.04	0.10	-0.07	0.10	0.00	0.14	0.07	0.16	0.01	0.17
MTBV	-0.02	0.04	-0.05	0.03	-0.06*	0.02	-0.31*	0.06	-0.31*	0.07	-0.31*	0.06
Coded familiarity	0.09	0.08	0.09	0.08	0.10	0.08	0.03	0.11	0.05	0.11	0.02	0.11
Coded reputation	-0.13	0.08	-0.04	0.10	-0.04	0.09	0.00	0.09	-0.03	0.09	0.03	0.10
Coded fine	0.35*	0.08	0.28*	0.07	0.28*	0.07	0.13	0.10	0.21	0.11	0.21*	0.10
Coded magnitude of act	0.22*	0.07	0.22*	0.07	0.22*	0.07	-0.01	0.08	0.04	0.08	0.01	0.08
Collection	-0.20*	0.08	-0.33*	0.09	-0.33*	0.09	0.22*	0.09	0.18*	0.08	0.13	0.10
Pro-org. unethical behavior ^a			-0.27*	0.06	-0.31*	0.07			0.06	0.09	0.24	0.14
Morality of organizational goals			-0.24*	0.10	-0.24*	0.09					-0.15	0.12
Pro-org. × org. morality					-0.11*	0.05					0.00	0.08
Moral judgments ^b									-0.20*	0.08	-0.08	0.11
Moral judgments × pro-org.											-0.30*	0.12
<i>R</i> ²	.40*		.49*		.50*		.23*		.27*		.30*	
ΔR^2			.09*		.01				.04*		.03*	

Note: ^a Lower values indicate pro-self unethical behavior; higher values indicate pro-organizational unethical behavior. ^b Higher values indicate an act being evaluated as more immoral; * *p* < .05. Robust standard errors with firm-level clustering. Abnormal returns are in percentages. Standardized measures are used.

Table 3 Study 2: Variable Means, Standard Deviations, Reliabilities, and Correlations (N = 920)

	M	SD	Min	Max	1	2	3	4	5	6
1. Pro-org. unethical behavior (Experimental Condition) ^a	0.50	0.50	0.00	1.00	-					
2. Morality of org. goals (Experimental Condition) ^b	0.50	0.50	0.00	1.00	0.00	-				
3. Pro-org. unethical behavior (Continuous)	3.74	2.33	1.00	7.00	0.88	-0.02	(.96)			
4. Morality of org. goals (Continuous)	3.92	1.90	1.00	7.00	-0.22	0.66	-0.20	(.97)		
5. Moral judgments ^c	6.32	1.06	1.00	7.00	-0.08	-0.06	-0.09	-0.02	(.96)	
6. Anticipated stock performance	-3.57	3.84	-10.00	9.00	-0.52	0.23	-0.52	0.35	-0.12	-

Note: Cronbach's α values are in brackets on the diagonal. ^a Dummy coded: 0 = Pro-self unethical behavior; 1 = Pro-organizational unethical behavior. ^b Dummy coded: 0 = Low morality of organizational goals; 1 = High morality of organizational goals. ^c Higher values indicate an act being evaluated as more immoral. All correlations above $|\text{.08}|$ are significant at $p < .05$.

Table 4 Study 2: Regression Analyses of Moral Judgments and Anticipated Stock Performance (continuous measures)

	Moral Judgments		Moral Judgments		Anticipated Stock Performance		Anticipated Stock Performance	
	Model 1a		Model 2a		Model 1b		Model 2b	
	<i>b</i>	<i>SE</i>	<i>b</i>	<i>SE</i>	<i>b</i>	<i>SE</i>	<i>b</i>	<i>SE</i>
Pro-org. unethical behavior ^a	-0.10*	0.02	0.10*	0.02	-0.53*	0.03	-0.52*	0.03
Morality of organizational goals	-0.03	0.03	0.04	0.03				
Pro-org. \times org. morality			-0.11*	0.03				
Moral judgments ^b					-0.17*	0.04	-0.16*	0.04
Moral judgments \times pro-org.							-0.07*	0.03
R^2	.01*		.03*		.29*		.30*	
ΔR^2			.02*				.01*	

Note: ^a Lower values indicate pro-self unethical behavior; higher values indicate pro-organizational unethical behavior. ^b Higher values indicate an act being evaluated as more immoral; $p < .05$. Robust standard errors with participant-level clustering. Standardized measures are used. We acknowledge that though significant, the ΔR^2 for Model 2a and 2b is small.