Title: Ethical Standards and Cultural Assimilation in Financial Services

Abstract: We introduce ethical agents into an analysis of decision making in a profit-maximising firm. Agents can adopt a profitable new practice that may harm customers. Their decision reflects moral considerations, organisational culture, and compensation contracts. We analyse both utilitarian and deontological (duty-based) philosophical traditions. Cultural assimilation emerges as an equilibrium phenomenon. With sophisticated customers, the principal enables a culture that achieves the highest possible aggregate surplus and, under deontological ethics, both the principal and the customers would prefer to deal with less ethically committed agents. In contrast, the principal designs compensation to enable cultures that exploit naïve customers.