# Business Ethics

## Decision Making for Personal Integrity & Social Responsibility

THIRD EDITION


Laura P. Hartman | Joseph DesJardins | Chris MacDonald

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**Laura P. Hartman**
*DePaul University*

**Joe DesJardins**
*College of St. Benedict/
St. John's University*

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To Rachel and Emma.

—Laura Hartman

To Michael and Matthew.

—Joe DesJardins

To Georgia.

—Chris MacDonald

# About the Authors

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Laura P. Hartman is Vincent de Paul Professor of Business Ethics and Legal Studies in DePaul University's Driehaus College of Business, serves as Special Assistant to the President with a focus on Haiti, and is also Research Director of DePaul's Institute for Business and Professional Ethics. Hartman also chairs the board of a trilingual elementary school in Haiti: the School of Choice/l'Ecole de Choix. Previously, Hartman was Director of External Partnerships for Zynga .org, through which Zynga players have contributed more than $14 million toward both domestic and international social causes. From 2009 to 2011, Hartman represented DePaul University on the steering committee for Zafen.org, a microfinance organization seeking to enhance economic development in Haiti to benefit Haitians living in poverty. She has been an invited professor at INSEAD (France), HEC (France), and the Université Paul Cezanne Aix Marseille III, among other European universities, and she previously held the Grainger Chair in Business Ethics at the University of Wisconsin–Madison. Her other books include *Rising above Sweatshops: Innovative Management Approaches to Global Labor Challenges, Employment Law for Business, Perspectives in Business Ethics,* and *The Legal Environment of Business: Ethical and Public Policy Contexts.* Hartman graduated from Tufts University and received her law degree from the University of Chicago Law School.

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Joe DesJardins is Vice Provost, as well as Professor in the Department of Philosophy, at the College of St. Benedict and St. John's University in Minnesota. His other books include: *An Introduction to Business Ethics, Environmental Ethics: An Introduction to Environmental Philosophy, Environmental Ethics: Concepts, Policy & Theory, Contemporary Issues in Business Ethics* (co-editor with John McCall), and *Business, Ethics, and the Environment: Imagining a Sustainable Future.* He is the former Executive Director of the Society for Business Ethics, and has published and lectured extensively in the areas of business ethics, environmental ethics, and sustainability. He received his B.A. from Southern Connecticut State University, and his M.A. and Ph.D. from the University of Notre Dame. He previously taught at Villanova University.

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Chris MacDonald is an Associate Professor in the Ted Rogers School of Management at Ryerson University in Toronto, Canada, and a Senior Fellow at Duke University's Kenan Institute for Ethics. His peer-reviewed publications range across business ethics, professional ethics, bioethics, the ethics of technology, and moral philosophy, and he is co-author of a best-selling textbook called *The Power of Critical Thinking* (3rd Canadian Edition, 2013). He has several times been declared one of the "100 Most Influential People in Business Ethics" by *Ethisphere* magazine. He is perhaps best known for his highly respected blog, *The Business Ethics Blog,* which is carried by *Canadian Business*.

# Preface

We began writing the first edition of this textbook in 2006, soon after a wave of major corporate scandals had shaken the financial world. Headlines made the companies involved in these ethical scandals household names: Enron, WorldCom, Tyco, Adelphia, HealthSouth, Global Crossing, Arthur Andersen, ImClone, KPMG, J.P. Morgan, Merrill Lynch, Morgan Stanley, Citigroup, Salomon Smith Barney, and even the New York Stock Exchange itself. At the time, we suggested that, in light of such significant cases of financial fraud, mismanagement, criminality and deceit, the relevance of business ethics could no longer be questioned.

Sadly, though we are now several editions into the publication, these very same issues are as much alive today as they were a decade ago—and decades prior to our original publication. While our second edition was preceded by the financial meltdown in 2008–2009 and the problems faced by such companies as AIG, Countrywide, Lehman Brothers, Merrill Lynch, and Bear Stearns, and of the financier Bernard Madoff, this current edition continues to witness financial and ethical malfeasance of historic proportions and the inability of market mechanisms, internal governance structures, or government regulation to prevent it.

As we reflect upon the ethical corruption and financial failures of the past decade, the importance of ethics is all too apparent. The questions today are less about whether ethics should be a part of business strategy and, by necessity, the business school curriculum, than about which values and principles should guide business decisions and *how* ethics should be integrated within business and business education.

This textbook provides a comprehensive yet accessible introduction to the ethical issues arising in business. Students who are unfamiliar with ethics will find that they are as unprepared for careers in business as students who are unfamiliar with accounting and finance. It is fair to say that students will not be fully prepared, even within traditional disciplines such as accounting, finance, human resource management, marketing, and management, unless they are sufficiently knowledgeable about the ethical issues that arise specifically within and across those fields.

While other solid introductory textbooks are available, several significant features make this book distinctive. We emphasize a **decision-making approach** to ethics, and we provide strong **pedagogical support** for both teachers and students throughout the entire book. In addition, we bring both of these strengths to the students through a pragmatic discussion of issues with which they are already often familiar, thus approaching them through subjects that have already generated their interest.

## New to the Third Edition

While our goal for the third edition remains the same as for the first—to provide "a comprehensive yet accessible introduction to the ethical issues arising in business"—you will notice a few changes. To begin, we are enthusiastic to introduce a third author to our mix, Dr. Chris MacDonald. You will find his complete biography elsewhere in the text. Inviting Dr. MacDonald to join our author team enriches the book's sense of hands-on reality. We believe that you will find that Dr. MacDonald, an influential thought leader in our field, has a remarkable ability to take today's complicated business transactions and help us to distill their complexities into completely understandable terms. Because we found ourselves often relying on his work to keep abreast of the latest happenings in business ethics, we thought it would be a good idea just to bring him aboard as a co-author! Gratefully, he was willing to join us.

While you might notice Dr. MacDonald's contributions throughout the text in terms of the *Reality Checks* and *Decision Points,* in particular, we have worked to enhance our focus on decision making as well as the emphasis on all elements on both personal and policy-level perspectives on ethics. We continue to provide pedagogical support throughout the text and, with Dr. MacDonald's contributions, we have provided many new versions of distinct items such as the *Reality Checks, Decision Points,* and a number of new readings to reflect new cases, examples, and up-to-the-minute data.

Among these changes are the following:

- More than 20 new end-of-chapter readings, averaging more than two new readings for each chapter.
- New readings offering international and global perspectives.
- New or updated cases to serve as Opening Decision Points in every chapter.
- New readings on stakeholder theory.
- Extremely timely and expanded textual coverage of such topics as the Enbridge oil spill in Canada's Northwest Territories, the MBA Oath, whistle-blowers, Goldman Sachs and corporate culture, social media and the employment context, bullying in the workplace, and the growing LIBOR scandal.

Finally, we have made numerous small editorial changes in each chapter to make the text more readable, to clarify concepts, to better integrate theory and practice, and to improve end-of-chapter questions to better support assessment of student learning, group projects, and classroom discussion.

# Acknowledgments

A textbook should introduce students to the cutting edge of the scholarly research that is occurring within a field. As in any text that is based in part on the work of others, we are deeply indebted to the work of our colleagues who are doing this research. We are especially grateful to those scholars who graciously granted us personal permission to reprint their materials in this text:

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Chapter 1

# Ethics and Business

All that is necessary for the triumph of evil is that good men do nothing.

*Edmund Burke 1729–1797*

Ethics is the new competitive environment.

*Peter Robinson, CEO Mountain Equipment Co-op*

Without commonly shared and widely entrenched moral values and obligations, neither the law, nor democratic government, nor even the market economy will function properly.

*Václav Havel 1936–2011*

No snowflake in an avalanche ever feels responsible.

*Voltaire*

# Opening Decision Point[1] *Selling Less Meat*

The term "business ethics" includes both words: ethics and business. The "ethics" element refers to the application of values within a business context. In the for-profit environment, the business context means that a firm must (usually) earn a profit in order to survive and to serve its mission. For well-intentioned companies, is there a tension between doing what they think is right and doing the things that customers are willing to pay them for?

Let us take a look at the case of a food company that attempted, very gently, to get its customers to eat less meat. The meat industry has faced plenty of criticism lately, given questions about animal suffering, environmental implications, and health impacts. The health impacts in question aren't just a concern for individuals. Society as a whole faces increased spending on health care, in part the result of poor diet. Saturated fats from meat are a part of the problem. Today, only about 3 percent of American adults are vegetarians, though of course many more claim to be trying to reduce the amount of meat in their diets. On the other hand, Americans are still one of the most meat-loving people on earth, consuming more meat per person than any other OECD (the Organisation for Economic Co-operation and Development) country except Luxembourg. Clearly, Americans as a nation have a complex relationship with meat consumption.

So the question arises: Do food companies have a social obligation to try to sell less meat? A 2011 effort by cafeteria services provider Sodexo, which serves more than 10 million meals each day in North America alone, illustrates this challenge. Sodexo, a publicly traded, multinational corporation with headquarters in France, is one of the largest food services companies in the world, with more than 33,000 sites spread across corporations, schools, government agencies, and hospitals around the world.[2] In 2011, Sodexo announced that it would participate in the "Meatless Monday" campaign, a nonprofit effort urging consumers to eliminate or reduce the amount of meat consumed just one relatively painless day each week. Sodexo's participation meant that the company's cafeterias began providing meat-free main dishes and main dishes with less meat, along with educational materials for customers.

As Sodexo contemplated launching the company's Meatless Monday experiment, there were several reasons to believe that the project could result in a best-case scenario of corporate social responsibility. Serving less meat is good for the environment, good for consumers' health, and (because meat is an expensive ingredient) possibly good for the bottom line. From both an ethics and a business point of view, it seemed like a reasonable marketing experiment.

Sodexo clearly wanted to do what is best for its customers, and for society more generally. But the company also had to take into consideration its obligation to give customers what they want, in order to continue making a profit. Listed here are some of the major challenges that Sodexo confronted. Are they insurmountable? Consider how you might resolve some of them. In this chapter, we will introduce a process by which to examine these types of dilemmas and then we will return to these questions at the end of the chapter.

1. Different people have different attitudes toward the ethics of producing, eating, and selling meat. Some people think it deeply unethical. Others think it not ethically problematic at all. Still others believe that we should reduce the

(*continued*)

(*concluded*)

amount of meat we eat, but not eliminate it from our diets altogether. For a company like Sodexo, with a broad customer base, this means that there is no clear social consensus to use as a guide for corporate policy.

2. Even if participating in the Meatless Monday program does not threaten Sodexo's survival, what if consumers do not appreciate the effort, and the program negatively affects profits? A profitable company like Sodexo can arguably stand to lose a small portion of its profit margin. Some people would say that profit reduction is justified in the pursuit of social goods, such as improved nutrition or reduced animal suffering. Of course, shareholders may disagree. It is not obvious how to balance small reductions in profit with a company's social obligations.
3. There's a saying that "the customer is always right." But clearly there are limits on what any responsible company is willing to sell—every company faces choices in this regard. Many food products are especially challenging that way, because there are foods that are harmless when consumed in moderation, but unhealthy when consumed in large quantities. It is not clear how much responsibility companies have for the choices consumers make.

**Source:** Adapted from Chris MacDonald, "Meatless Monday and Corporate Social Responsibility," *Canadian Business* [Blog], April 13, 2012, www.canadianbusiness.com/blog/business_ethics/79702 (accessed July 19, 2012).

## Chapter Objectives

After reading this chapter, you will be able to:

1. Explain why ethics is important in the business environment.
2. Explain the nature of business ethics as an academic discipline.
3. Distinguish the ethics of personal integrity from the ethics of social responsibility.
4. Distinguish ethical norms and values from other business-related norms and values.
5. Distinguish legal responsibilities from ethical responsibilities.
6. Explain why ethical responsibilities go beyond legal compliance.
7. Describe ethical decision making as a form of practical reasoning.

# Introduction: Making the Case for Business Ethics

Even though years have passed and other scandals have occurred, we still refer to the 2001 Enron Corporation collapse as the watershed event in this century's business ethics news; since that time ethics and values have seldom strayed from the front pages of the press. Recall the 2008 collapse of the investment schemes of former NASDAQ chairman Bernie Madoff, the largest fraud of its kind in history with total losses to investors in the billions. Whether we are referring to government scandals such as Illinois governor Rod Blagojevich's conviction for attempting to auction President Obama's senate seat to the highest bidder or to the federal bailout following the mortgage crisis, the list of leaders that have been involved with legal and ethical wrongdoing is, sadly, incredibly long. Reflect for a moment on the businesses that have been involved in scandals or, at least, in flawed decision making since the start of the 21st century: Siemens, Enron, Halliburton, AIG, WorldCom, Tyco, Adelphia, Cendant, Rite Aid, Sunbeam, Waste Management, HealthSouth, Global Crossing, Arthur Andersen, Ernst & Young, Imclone, KPMG, J.P. Morgan, Merrill Lynch, Morgan Stanley, Bear Stearns, Fannie Mae, Countrywide Financial Corp., Citigroup, Salomon Smith Barney, Marsh & McLennan, Credit Suisse First Boston, Goldman Sachs, Ameriquest, Deutsche Bank, WaMu, Bank of America, UBS, Standard and Poor's, Moody's, BP Global, Deep Water Horizon, Johnson & Johnson, Pfizer, Firestone Tire and Rubber Company, and even the New York Stock Exchange itself. Individuals implicated in ethical scandals include Kenneth Lay, Jeffrey Skilling, Andrew Fastow, Dennis Kozlowski, Bill McGuire, Bob Nardelli, John J. Rigas, Richard M. Scrushy, Martha Stewart, Samuel Waksal, Richard Grasso, Bernard Ebbers, Angelo Mozilo, Kerry Killinger, Stephen Rotella, David Schneider, Fabrice Tourre, Richard J. Fuld, Vikrim Pandit, and Bernie Madoff. Beyond these well-known scandals, consumer boycotts based on allegations of unethical conduct or alliances have targeted such well-known firms as Nike, McDonald's, Carrefour, Home Depot, Chiquita Brands International, Fisher-Price, Gap, Shell Oil, ExxonMobil, Levi Strauss, Donna Karan, Kmart, Walmart, Nestle, Nokia, Siemens, BP, H&M, Target, Timberland, and Delta Airlines.

This chapter will introduce business ethics as a process of responsible decision making. Simply put, the scandals and ruin experienced by all the institutions and every one of the individuals just mentioned were brought about by *ethical failures*. If we do, indeed, reflect on those institutions and individuals, perhaps they should remind us of the often-repeated Santayana admonition, "Those who cannot remember the past are condemned to repeat it."[3] This text provides a decision-making model that, we contend, can help individuals to understand these failures and to avoid future business and personal tragedies. As an introduction to that decision-making model, this chapter reflects on the intersection of ethics and business.

Ethical decision making in business is not at all limited to the type of major corporate decisions with dramatic social consequences listed earlier. At some point, every worker, and certainly everyone in a management role, will be faced with an issue that will require ethical decision making. Not every decision can be covered by economic, legal, or company rules and regulations. More often than not, responsible decision making must rely on the personal values and principles of the individuals involved. Individuals will have to decide for themselves what type of person they want to be.

At other times, of course, decisions will involve significant general policy issues that affect entire organizations, as happened in all the well-known corporate scandals. The managerial role especially involves decision making that establishes organizational precedents and has organizational and social consequences. Hence, both of these types of situations—the personal and the organizational—are reflected in the title of this book: *Business Ethics: Decision Making for Personal Integrity and Social Responsibility.*

How should we conceive of the relationship between business and market activity, on the one hand, and ethical concerns, on the other? This is not a new question, but one that can be found since the very dawn of modern capitalism. Often considered to be the founding father of laissez-faire economics, the 18th-century philosopher Adam Smith is best known for expounding the virtues of self-interest in *The Wealth of Nations*. However, in another of his major works, *The Theory of Moral Sentiments,* Smith suggests that sympathy and benevolence are fundamental human values. The relationship between these two texts has long puzzled scholars, and has come to represent the broader issue of the relationship of economic and moral values that is addressed in the study of business ethics. As one commentator writes, "The Adam Smith problem—how to reconcile these two great books—is also the challenge of how to order a society in which competition and ethical sensibility are combined."[4]

As recently as the mid-1990s, articles in such major publications as *The Wall Street Journal,* the *Harvard Business Review,* and *U.S. News and World Report* questioned the legitimacy and value of teaching classes in business ethics. Few disciplines face the type of skepticism that commonly confronted courses in business ethics. Many students believed that "business ethics" was an oxymoron. Many also viewed ethics as a mixture of sentimentality and personal opinion that would interfere with the efficient functioning of business. After all, who is to identify right and wrong, and, if no law is breached, who will "punish" the "wrongdoers?" However, this approach has left business executives as one of the lowest ranked professions in terms of trust and honesty, according to a 2011 Gallup poll.[5]

Leaders realize that they can no longer afford this approach in contemporary business. The direct costs of unethical business practice are more visible today than perhaps they have ever been before. As discussed earlier, the first decade of the new millennium has been riddled with highly publicized corporate scandals, the effects of which did not escape people of any social or income class. Moreover, we saw the economy begin a downward spiral into one of the largest financial crises of the last 80 years, driven significantly by questionable sub-prime mortgage lending practices at the banks, as well as the widespread trading of risky mortgage-backed securities in the markets. These lending and trading efforts encouraged bad debt to appreciate beyond levels that the market could bear. The inevitable correction caused real estate values in most markets to decline sharply, domestic credit markets to freeze, and the federal government to intervene with a rescue package.

If the key (or not so key) decision makers who contributed to the bubble bursting had acted differently, could these unfortunate consequences have been avoided? Well, suffice it to say that it is a bit of a vicious circle. Economic turmoil incites misconduct; there is a significant *bump* in observed workplace misconduct during times of economic challenges. Some money-saving strategies deployed by struggling companies, such as compensation/benefit reductions and hiring freezes, have been found to increase misconduct by more than 35 percent.[6] In turn, misconduct based on fraud alone causes an estimated 5 percent loss of annual revenues, equivalent to more than $2.9 trillion of the 2009 gross world product.

Personal retirement accounts like 401ks, institutional investments like pension funds, federal, state, and municipal retirement funds, and major insurance companies are heavily invested in corporate stocks and bonds, as well as pooled securities of every size, shape, and order. As a result, these costs of Wall Street failures on Main Street families and businesses become larger and more noticeable by the day.

The questions today are less about *why* or *should* ethics be a part of business; they are about *which* values and principles should guide business decisions and *how* ethics should be integrated within business. (A persuasive case for *why* this shift has occurred can be found in the reading "Value Shift," by Lynn Sharp Paine.) Students unfamiliar with the basic concepts and categories of ethics will find themselves as unprepared for careers in business as students who are unfamiliar with accounting and finance. Indeed, it is fair to say that students will not be fully prepared, even within fields such as accounting, finance, human resource management, marketing, and management, unless they are familiar with the ethical issues that arise within those specific fields.

Consider the ethical implications of the legal and market-based decisions that are discussed in the Heath reading at the end of the chapter. Our individual choices are restricted, but only to certain extents. Beyond those parameters, we must rely on ethical judgment to reach decisions that fall squarely within the field traditionally described as business-related. Yet, at the same time, our personal ethics also are challenged. While we will return to this tension in chapter 2, the concept of a personal standard is paramount, and the readings by both MacDonald and Vermaelen examine the potential, for instance, of the MBA Oath as one way to resolve these challenges.

1 OBJECTIVE

To understand the origins of this shift from *whether* ethics or values should play a role in business decisions to the almost frantic search for *how* most effectively (and quickly!) to do it, consider the range of people who were harmed by Bernie Madoff's pyramid investment scheme. The largest security fraud in history, Madoff's unethical behavior led to cash losses of at least $20 billion for his clients. Though much of the media's initial attention focused on the big banks, wealthy hedge fund managers, and Hollywood celebrities defrauded by Madoff, the impact of his crimes was felt far beyond this small circle. More than 100 nonprofit organizations—including the New York Public Library, the Children's Health Fund, and a neurological research center at the Massachusetts Institute of Technology—had vested assets with Madoff's fund and were forced to curtail or eliminate services as a result of the collapse. The charitable foundation founded by Holocaust survivor and Nobel laureate Elie Wiesel was just one of many nonprofits that were wiped out entirely. The scandal led to the financial devastation of pension funds, hospitals, and universities across the globe, as well as to the bankruptcies of several smaller banks. In each case of economic loss, communities of the investing group or individual were negatively affected by the loss, and the families of those affected suffered hardship. Many of the individuals directly involved in Madoff's fund have since suffered criminal and civil punishment, up to and including prison sentences for some. Indeed, it is hard to imagine anyone who was even loosely affiliated with Madoff who was not harmed as a result of the ethical failings there. Multiply that harm by the dozens of other companies implicated in similar scandals to get a better idea of why ethics is no longer dismissed as irrelevant. The consequences of unethical behavior and unethical business institutions are too serious for too many people to be ignored.

This description of the consequences of the Madoff Ponzi scheme demonstrates the significant impact that business decisions can have on a very wide range of people. Madoff's choices dramatically affected the lives of thousands of people: investors, businesses, schools, nonprofit organizations, retirees, and the communities in which these people live. For better or for worse, the decisions that a business makes will affect many more people than just the decision maker. As we will discuss throughout this text, in order to sustain the firm, ethically responsible business decision making must move beyond a narrow concern with stockholders to consider the impact that decisions will have on a wide range of **stakeholders.** In a general sense, a business *stakeholder* will be anyone who affects or is affected by decisions made within the firm, for better or worse. Failure to consider these additional stakeholders will have a detrimental impact on those stakeholders, on stockholders, specifically, and on the firm's long-term sustainability as a whole. This perspective is articulated effectively by Whole Foods Supermarket's "Declaration of Interdependence."

> Satisfying all of our stakeholders and achieving our standards is our goal. One of the most important responsibilities of Whole Foods Market's leadership *is to make sure the interests, desires and needs of our various stakeholders are kept in balance.* We recognize that this is a dynamic process. It requires participation and communication by all of our stakeholders. It requires listening compassionately, thinking carefully and acting with integrity. Any conflicts must be mediated and win-win solutions found. Creating and nurturing this community of stakeholders is critical to the long-term success of our company. (Emphasis added.)[7]

Whole Foods has maintained this priority structure over a period of 15 years, during which it has performed extremely well for its shareholders. In fiscal year 2011, the company had sales of approximately $10 billion and more than 300 stores in the United States, Canada, and the United Kingdom.[8]

The Reality Check, "Why Be Ethical? Because the Law Requires It" describes some legal requirements that have been created since the Enron fiasco. Beyond these specific legal obligations, organizational sustainability is reliant on ethical decisions in myriad ways. Unethical behavior not only creates legal risks for a business, it creates financial and marketing risks as well. Managing these risks requires managers and executives to remain vigilant about their company's ethics. It is now clearer than ever that a company can lose in the marketplace, go out of business, and its employees go to jail if no one is paying attention to the ethical standards of the firm.

## Reality Check *Why Be Ethical? Because the Law Requires It*

Today, business executives have many reasons to be concerned with the ethical standards of their organizations. Perhaps the most straightforward reason is that the law requires it, often as a minimum. In 2002, the U.S. Congress passed the Sarbanes-Oxley Act to address the wave of corporate and accounting scandals. Section 406 of that law, "Code of Ethics for Senior Financial Officers," requires that corporations have a Code of Ethics "applicable to its principal financial officer and comptroller or principal accounting officer, or persons performing similar functions." The Code must include standards that promote:

1. Honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships.
2. Full, fair, accurate, timely, and understandable disclosure in the periodic reports required to be filed by the issuer.
3. Compliance with applicable governmental rules and regulations.

*Note that you will see "Reality Checks" throughout each chapter in the text. Slightly different from Decision Points, these boxed additions offer practical applications of the concepts discussed during that chapter segment or examples of the ways in which the concepts are implemented in "real" business decision making.

Moreover, given the declining average life expectancy of firms,[9] maintaining an ethical advantage becomes a vital distinction between successful and unsuccessful firms. A firm's ethical reputation can provide a competitive edge in the marketplace with customers, suppliers, and employees. On the positive side, managing ethically can also pay significant dividends in organizational structure and efficiency. Trust, loyalty, commitment, creativity, and initiative are just some of the organizational benefits that are more likely to flourish within ethically stable and credible organizations (see the Reality Check, "Why Be Good?"). Research demonstrates that 94 percent of workers consider a firm's ethics critically important in their choice of employers. In fact, 82 percent of employees say that they would prefer a position at lower pay in a firm with ethical business practices compared to a higher paying job at a company with questionable ethics. Further, one-third of U.S. workers have walked off of a job on the basis of their ethics.[10] Alternatively, the consumer boycotts of such well-known firms as Nike, McDonald's, Home Depot, Fisher-Price, and Walmart, mentioned previously, give even the most skeptical business leader reason to pay attention to ethics.

For business students, the need to study ethics should be as clear as the need to study the other subfields of business education. As discussed earlier, without this background, students simply will be unprepared for a career in contemporary business. But even for students who do not anticipate a career in business management or business administration, familiarity with business ethics is just as crucial. After all, it was not only Bernie Madoff who suffered because of his ethical lapses. Our lives as employees, as consumers, and as citizens are affected by decisions made within business institutions; therefore, everyone has good reasons for being concerned with the ethics of those decision makers.

**Reality Check** *Why Be Good?*

The Aveta Business Institute provides the following tips on the "The Importance and Advantages of Good Business Ethics":

Companies with good ethical policies enjoy the following benefits:

- Marketing advantages over their competitors through improved customer loyalty.
- Improved employee morale.
- Improved reputation management through avoidance of scandal.
- Good standing in the eyes of regulatory bodies.

**Source:** Aveta Business Institute, http://www.sixsigmaonline.org/six-sigma-training-certification-information/the-importance-and-advantages-of-good-business-ethics.html (accessed May 15, 2012).

Moreover, as leaders and as emerging leaders, we need to explore how to manage the ethical behavior of others so that we can impact their decisions and encourage them to make ethical, or more ethical, decisions. Certainly, unethical behavior continues to permeate organizations today at all levels; and business decision makers—at all levels—must be equipped with the tools, the knowledge, and the skills to confront that behavior and to respond to it summarily. Just imagine the impact in terms of role modeling of this single statement by Prince Bandar Bin Sultan, in connection with allegations that he received secret and personal "commissions" of approximately $240 million each over a 10-year period in connection with a defense contract between the British government and the Saudi arms manufacturer, BAE Systems:

> *[T]he way I answer the corruption charges is this. In the last 30 years, . . . we have implemented a development program that was approximately, close to $400 billion worth. You could not have done all of that for less than, let's say, $350 billion. Now, if you tell me that building this whole country and spending $350 billion out of $400 billion, that we had misused or got corrupted with $50 billion, I'll tell you, 'Yes.' But I'll take that any time.*
>
> *But more important, who are you to tell me this? I mean, I see every time all the scandals here, or in England, or in Europe. What I'm trying to tell you is, so what? We did not invent corruption. This happened since Adam and Eve. I mean, Adam and Eve were in heaven and they had hanky-panky and they had to go down to earth. So I mean this is—this is human nature. But we are not as bad as you think!*[11]

In that case, British Prime Minister Tony Blair had originally allowed the fraud investigation to be dropped. He offered the following statement, in an effort to explain his reasons for the decision: "This investigation, if it had gone ahead, would have involved the most serious allegations in investigations being made into the Saudi royal family. My job is to give advice as to whether that is a sensible thing in circumstances where I don't believe the investigation incidentally would have led anywhere except to the complete wreckage of a vital strategic relationship for our country. . . . Quite apart from the fact that we would have lost thousands, thousands of British jobs."[12]

Some observers may look to the choices made in late 2008 and 2009 by American International Group (AIG), the world's largest insurer, as another example of poor role modeling. One can easily see the impact of those decisions on reputation. In September 2008, AIG was on the brink of bankruptcy. There was a realistic fear that if the company went under the stability of the U.S. markets may have been in serious jeopardy. Over a five-month period, the U.S. government bailed out AIG to the tune of $152.2 billion (funded by U.S. tax dollars) in order to keep the company afloat, because AIG arguably was "too big to fail."

While that consequence alone was unfortunate, it certainly was not unethical. However, in decisions that damaged the reputations of many involved, among other charges, one month after AIG received the first round of bailout money, its executives headed to California for a weeklong retreat at an extremely luxurious hotel, with the company covering the nearly half a million dollar tab *with the bailout money.* Six months later, these same executives rewarded themselves with bonuses totaling over $100 million. Although President Obama (some say belatedly) derided the executives for their legally-awarded bonuses, many of the bonuses were paid nevertheless because they had been promised through employee contracts before AIG had received any bailout money for the purposes of "retaining talent."[13]

While it did not reach full congressional hearing, the House even prepared a bill that would impose a 90 percent tax on the bonuses paid to executives by AIG and other companies that were getting assistance from the government of more than $5 million. Instead, the House passed the Grayson-Himes Pay for Performance Act in April 2009, "to amend the executive compensation provisions of the Emergency Economic Stabilization Act of 2008 to prohibit unreasonable and excessive compensation and compensation not based on performance standards."[14] This bill would ban future "unreasonable and excessive" compensation at companies receiving federal bailout money. Treasury secretary Timothy Geithner would have the power to define what constitutes reasonable compensation and to review how companies give their bonuses.

The case for business ethics is clear and persuasive. Business must take ethics into account and integrate ethics into its organizational structure. Students need to study business ethics. But what does this mean? What is "*ethics,*" and what is the objective of a class in business ethics?

## Business Ethics as Ethical Decision Making

As the title of this book suggests, our approach to business ethics will emphasize **ethical decision making.** No book can magically create ethically responsible people or change behavior in any direct way. But students can learn and practice responsible and accountable ways of thinking and deliberating. We assume that decisions that follow from a process of thoughtful and conscientious reasoning will be more responsible and ethical. In other words, *responsible decision making and deliberation will result in more responsible behavior.*

So what is the point of a business ethics course? On one hand, "ethics" refers to an academic discipline with a centuries-old history; we might expect knowledge about this history to be among the primary goals of a class in ethics. Thus, in an ethics course, students might be expected to learn about the great ethicists of history such as Aristotle, John Stuart Mill, and Immanuel Kant. As in many other courses, this approach to ethics would focus on the *informational content* of the class.

2 OBJECTIVE

Yet, according to some observers, ethical theories and the history of ethics is beside the point. These stakeholders, including some businesses looking to hire college graduates, business students, and even some teachers themselves, expect an ethics class to address ethical *behavior,* not just information and knowledge about ethics. After all, what good is an ethics class if it does not help prevent future Madoffs? For our purposes, **ethics** refers not only to an academic discipline, but to that arena of human life studied by this academic discipline, namely, *how human beings should properly live their lives.* An ethics course will not change your capacity to think, but it could stimulate your choices of what to think about.

A caution about influencing behavior within a classroom is appropriate here. Part of the hesitation about teaching ethics involves the potential for abuse; expecting teachers to influence behavior could be viewed as permission for teachers to impose their own views on students. To the contrary, many believe that teachers should remain value-neutral in the classroom and respect a student's own views. Another part of this concern is that the line between motivating students and manipulating students is a narrow one. There are many ways to influence someone's behavior, including threats, guilt, pressure, bullying, and intimidation. Some of the executives involved in the worst of the recent corporate scandals were very good at using some of these methods to motivate the people who worked for them. Presumably, none of these approaches belong in a college classroom, and certainly not in an ethical classroom.

But not all forms of influencing behavior raise such concerns. There is a major difference between manipulating someone and persuading someone, between threatening (unethical) and reasoning (more likely ethical). This textbook resolves the tension between knowledge and behavior by emphasizing ethical judgment, ethical deliberation, and ethical decision making. In line with the Aristotelian notion that "we are what we repeatedly do," we agree with those who believe that an ethics class should strive to produce more ethical *behavior* among the students who enroll. But we believe that the only academically and ethically legitimate way to achieve this objective is through careful and reasoned decision making. Our fundamental assumption is that a process of rational decision making, a process that involves careful thought and deliberation, can and will result in behavior that is more reasonable, accountable, and ethical.

Perhaps this view is not surprising after all. Consider any course within a business school curriculum. Few would dispute that a management course aims to create better managers. We would judge as a failure any finance or accounting course that denied a connection between the course material and financial or accounting practice. Every course in a business school assumes a connection between what is taught in the classroom and appropriate business behavior. Classes in management, accounting, finance, and marketing all aim to influence students' behavior. We assume that the knowledge and reasoning skills learned in the classroom will lead to better decision making and, therefore, better behavior within a business context. A business ethics class follows this same approach.

While few teachers think that it is our role to *tell* students the right answers and to *proclaim* what students ought to think and how they ought to live, still fewer think that there should be no connection between knowledge and behavior. Our role should not be to preach ethical dogma to a passive audience, but instead to treat students as active learners and to engage them in an active process of thinking, questioning, and deliberating. Taking Socrates as our model, philosophical ethics rejects the view that passive obedience to authority or the simple acceptance of customary norms is an adequate ethical perspective. Teaching ethics must, in this view, challenge students to *think for themselves.*

## Business Ethics as Personal Integrity and Social Responsibility

Another element of our environment that affects our ethical decision making and behavior involves the influence of social circumstances. An individual may have carefully thought through a situation and decided what is right, and then may be motivated to act accordingly. But the corporate or social context surrounding the individual may create serious barriers to such behavior. As individuals, we need to recognize that our social environment will greatly influence the range of options that are open to us and can significantly influence our behavior. People who are otherwise quite decent can, under the wrong circumstances, engage in unethical behavior while less ethically-motivated individuals can, in the right circumstances, do the "right thing." Business leaders, therefore, have a responsibility for the business environment that they create; we shall later refer to this environment as the "corporate culture." The environment can, therefore, strongly encourage or discourage ethical behavior. Ethical business leadership is precisely this skill: to create the circumstances within which good people are able to do good, and bad people are prevented from doing bad.

The Enron case provides an example. Sherron Watkins, an Enron vice president, seemed to understand fully the corruption and deception that was occurring within the company; and she took some small steps to address the problems within the Enron environment. But when it became clear that her boss might use her concerns against her, she backed off. The same circumstances were involved in connection with some of the Arthur Andersen auditors. When some individuals raised concerns about Enron's accounting practices, their supervisors pointed out that the $100 million annual revenues generated by the Enron account provided good reason to back off. The "Sherron Watkins" Decision Point exemplifies the culture present at Enron during the heat of its downfall.

# Decision Point

## *Sherron Watkins*

Following is a portion of a memo that Sherron Watkins, an Enron vice president, sent to CEO Kenneth Lay as the Enron scandal began to unfold. As a result of this memo, Watkins became infamous as the Enron "whistleblower."

> Has Enron become a risky place to work? For those of us who didn't get rich over the last few years, can we afford to stay? Skilling's [former Enron CEO Jeffrey Skilling] abrupt departure will raise suspicions of accounting improprieties and valuation issues. . . . The spotlight will be on us, the market just can't accept that Skilling is leaving his dream job. . . . It sure looks to the layman on the street that we are hiding losses in a related company and will compensate that company with Enron stock in the future. . . .
>
> I am incredibly nervous that we will implode in a wave of accounting scandals. My eight years of Enron work history will be worth nothing on my résumé, the business world will consider the past successes as nothing but an elaborate accounting hoax. Skilling is resigning now for "personal reasons" but I would think he wasn't having fun, looked down the road and knew this stuff was unfixable and would rather abandon ship now than resign in shame in two years.
>
> Is there a way our accounting gurus can unwind these deals now? I have thought and thought about a way to do this, but I keep bumping into one big problem—we booked the Condor and Raptor deals in 1999 and 2000, we enjoyed wonderfully high stock price, many executives sold stock, we then try and reverse or fix the deals in 2001, and it's a bit like robbing the bank in one year and trying to pay it back two years later. Nice try, but investors were hurt, they bought at $70 and $80 a share looking for $120 a share and now they're at $38 or worse. We are under too much scrutiny and there are probably one or two disgruntled "redeployed" employees who know enough about the "funny" accounting to get us in trouble. . . . I realize that we have had a lot of smart people looking at this and a lot of accountants including AA & Co. [Arthur Andersen] have blessed the accounting treatment. None of that will protect Enron if these transactions are ever disclosed in the bright light of day. (Please review the late 90's problems of Waste Management (news/quote)—where AA paid $130 million plus in litigation re questionable accounting practices.) . . .
>
> I firmly believe that executive management of the company must . . . decide one of two courses of action: 1. The probability of discovery is low enough and the estimated damage too great; therefore we find a way to quietly and quickly reverse, unwind, write down these positions/transactions. 2. The probability of discovery is too great, the estimated damages to the company too great; therefore, we must quantify, develop damage containment plans and disclose. . . . I have heard one manager-level employee from the principal investments group say, "I know it would be devastating to all of us, but I wish we would get caught. We're such a crooked company." These people know and see a lot.[15]

After the collapse of Enron, Watkins was featured on the cover of *Time* magazine and honored as a corporate whistleblower, despite the fact that she never shared these concerns with anyone other than Kenneth Lay. Yet, it surely took a great deal of courage within the Enron culture even to voice (write) what she wrote here, especially because no one else dared to mention it. How do we reach a judgment about Watkins' actions in this situation?

(*continued*)