JOSEPH W. WEISS

BUSINESS ETHICS

A Stakeholder and Issues Management Approach

- Cases
- Principles
- Practices

SIXTH EDITION

BUSINESS ETHICS

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A Stakeholder and Issues Management Approach

SIXTH EDITION

Joseph W. Weiss

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Business Ethics

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Preface

The sixth edition of *Business Ethics: A Stakeholder and Issues Management Approach* continues the mission of providing a practical, easy-to-read, engaging and contemporary text with detailed real-time contemporary and classic cases for students. This text updates the previous edition, adding fourteen new cases in addition to other new features discussed below.

We continue our quest to assist colleagues and students in understanding the changing environment from combined stakeholder and issues management approaches, based on the theory and practice that firms depend on stakeholders as well as stockholders for their survival and success. Acting morally while doing business is no longer a joking or even questionable topic of discussion. With the near shutdowns of the U.S. government, the subprime lending crisis, global climate changes, the fading middle class in America and other countries, China's continuing economic expansion, and India's inroads into the global economy, the stakes for the global economy are not trivial. Ethical behaviors are required, not optional, for this and future generations. Learning to think and reason ethically is the first step.

Business ethics is concerned with doing what is right over what is wrong, while acting in helpful over harmful ways, and with seeking the common good as well as our own welfare. This text addresses this foundational way of thinking by asking why does the modern corporation exist in the first place? What is its raison d'être? How does it treat its stakeholders? Business ethics engages these essential questions, and it is also about the purpose, values, and transactions of and between individuals, groups, and companies and their global alliances. Stakeholder theory and management, in particular, are what concern nonfinancial as well as the financial aspects of business behavior, policies, and actions. A stakeholder view of the firm complements the stockholder view and includes all parties and participants who have an interest—a stake—in the environment and society in which business operates.

Students and professionals need straightforward frameworks to thoughtfully and objectively analyze and then sort through complex issues in order to make decisions that matter—ethically, economically, socially, legally, and spiritually. The United States and indeed the whole world are different after the 9/11 attacks. Terrorism is a threat to everyone, everywhere, as the Boston bombings showed. Also threatening are the ongoing corporate scandals, the consequences of the Arab Spring, security issues worldwide, immigration problems, the inequalities in income distribution and wealth, the decay of the middle classes—all of these affect graduating students and those who wish to attend a university or college but cannot afford to. Business ethics affects our professional and personal relationships, careers, and lives, and this text attempts to identify and help analyze many of these issues and opportunities for change, using relevant ethical frameworks and reasoning.

The New Revised Sixth Edition: Why and How This Text Is Different

This edition builds on previous success factors to provide:

1. A competent, contemporary text grounded in factual and detailed research, while being easy to read and applying concepts and methods to real-time business-related situations.
2. Interesting and contemporary news stories, exercises, and examples.
3. In-depth, real-time customized cases (twenty-three in this edition) specifically designed for this book.
4. Ethical dilemmas experienced by real individuals, not hypothetical stories.
5. A detailed chapter on both stakeholder and issues management methods, with step-by-step explanations, not summarized or theoretical abstractions.
6. A straightforward business and managerial perspective supported by the latest research—not only a philosophical approach.
7. One of the most comprehensive texts on the topics of workforce and workplace demographics, generational trends, and issues relating to ethical issues.
8. Comprehensive coverage of the Sarbanes-Oxley Act, federal sentencing guidelines, and codes of conduct.
9. Personal, professional, organizational, and global perspectives, and information and strategies for addressing ethical dilemmas.
10. A decision-maker role for students in exercises and examples.

This edition adds features that enhance your ethical understanding and interest in contemporary issues in the business world. It also aligns even more closely with international Association to Advance Collegiate Schools of Business (AACSB) requirements to help students, managers, and leaders achieve in their respective fields. Additions and changes include:

- A Point/CounterPoint exercise has been added to several chapters to challenge students' thinking and arguments on contemporary issues. Topics include "too big to fail" (TBTF) institutions; advertising on the Boston bomber; student loan debt; and file sharing and other forms of online sharing.
- Twenty-three cases, of which fourteen are new and three updated, dealing with national and international issues.
- Updated national ethics survey data is included throughout the text.
- New perspectives on generational differences and ethical workplace issues have been added.
- Each chapter has new and updated lead-off cases and scenarios to attract students' attention.
- Updated data on global and international issues.
- Updated research and business press findings and stories have been added to each chapter to explain concepts and perspectives.

- Chapter 1 includes a section on personal ethics with Covey's maturity continuum and cases on cyberbullying and Madoff's Ponzi scheme.
- Chapter 2 now covers more material on personal ethics and has a section explaining the foundations of ethics with cases on Jerome Kerviel, rogue trader, Sam Waksal (ImClone), and the Ford Pinto.
- Chapter 3 is now the stakeholder and issues management chapter with a section explaining stakeholder theory in more depth with a lead-in case on the BP oil spill and aftermath in the Gulf of Mexico. Cases include genetic discrimination and the Mattel toy recalls.
- Chapter 4 has updated research throughout with new Ethical Insight inserts and cases on conscious capitalism, Goldman Sachs, and Google Books.
- Chapter 5 includes cases on fracking, for-profit education, neuromarketing, and gender discrimination.
- Chapter 6 includes new cases on Kaiser Permanente, and social networking and social responsibility.
- Chapter 7 remains a leader in the field on depth and coverage of current trends on generational differences, gender, and population changes. Cases include Facebook and Preemployment, and women on Wall Street.
- Chapter 8 features new research on skills and ethical capacities in international/global management and leadership. The "dark side" of globalization is updated with research on ethical issues in developing and underdeveloped countries. Cases include sweatshops and the U.S. industrial food system.

An Action Approach

The sixth edition puts the students in the decision-maker role when identifying and addressing ethical dilemmas with thought-provoking cases and discussion questions that ask, "What would you do if you had to decide a course of action?" Readers are encouraged to articulate and share their decision-making rationales and strategies. Readers will also learn how to examine changing ethical issues and business problems with a critical eye. We take a close look at the business reporting of the online editions of the *Wall Street Journal*, *60 Minutes*, the *New York Times*, *Businessweek*, the *Economist*, and other sources.

Stakeholder and Issues Management Analysis

Stakeholder analysis is one of the most comprehensive approaches for identifying issues, groups, strategies, and outcomes. In the sixth edition, these methods are presented in an updated and more integrative Chapter 3. This chapter offers a useful starting point for mapping the who, what, when, where, why, and how of ethical problems relating to organizations and their stakeholders. Issues and crisis management frameworks are explained and integrated into

approaches that complement the stakeholder analysis. Quick tests and negotiation techniques are presented in Chapters 2 and 8.

- A new instructor's manual and PowerPoints.
- Streamlined case teaching notes.
- Suggested videos and web sites for each chapter.

Objectives and Advantages of This Textbook

- To use an *action-oriented* stakeholder and issues management approach for understanding the ethical dimensions of business, organizational, and professional complex issues, crises, and events that are happening now.
- To introduce and *motivate students* about the relevance of ethical concepts, principles, and examples through actual moral dilemmas that are occurring in their own lives, as well as with known national and international people, companies, and groups.
- To present a *simple, straightforward* way of using stakeholder and issues management methods with ethical reasoning in the marketplace and in workplace relationships.
- To *engage and expand* readers' awareness of ethical and unethical practices in business at the individual, group, organizational, and multinational levels through *real-time*—not hypothetical—ethical dilemmas, stories, and cases.
- To instill *self-confidence and competence* in the readers' ability to think and act according to moral principles. The classroom becomes a lab for real-life decisions.

Structure of the Book

- Chapter 1 defines business ethics and familiarizes the reader with examples of ethics in business practices, levels of ethical analysis, and what can be expected from a course in business ethics. A Point/CounterPoint exercise engages students immediately.
- Chapter 2 has exchanged positions in the text with the former Chapter 3. This chapter engages students in a discussion of ethics at the personal, professional, organizational, and international levels. The foundations of ethical principles are presented in context with contemporary ethical decision-making approaches. Individual styles of moral decision making are also discussed in this section. Although the approach here is a micro-level one, these principles can be used to examine and explain corporate strategies and actions as well. (Executives, managers, employees, coalitions, government officials, and other external stakeholder groups are treated as individuals.)
- Chapter 3 introduces action-oriented methods for studying social responsibility relationships at the individual employee, group, and

organizational levels. These methods provide and encourage the incorporation of ethical principles and concepts from the entire book.

- Chapter 4 presents ethical issues and problems that firms face with external consumers, government, and environmental groups. How moral can and should corporations be and act in commercial dealings? Do corporations have a conscience? Classic and recent crises resulting from corporate and environmental problems are covered.
- Chapter 5 explains ethical problems that consumers face in the marketplace: product safety and liability, advertising, privacy, and the Internet. The following questions are addressed: How free is "free speech"? How much are you willing to pay for safety? Who owns the environment? Who regulates the regulators in an open society?
- Chapter 6 presents the corporation as internal stakeholder and discusses ethical leadership, strategy, structure, alliances, culture, and systems as dominant themes regarding how to lead, manage, and be a responsible follower in organizations today.
- Chapter 7 focuses on the individual employee stakeholder and examines the most recent, new and changing workforce/workplace trends, moral issues, and dilemmas employees and managers face and must respond to in order to survive and compete in national and global economies. This chapter has been described as a "must-read" for every human resource professional.
- Chapter 8 begins by asking students if they are ready for professional international assignments. Ethical and leadership competencies of new entrants into the global workforce are introduced, before moving the discussion to global and multinational enterprises (MNEs) and ethical issues between MNEs, host countries, and other groups. Issues resulting from globalization are presented along with stakeholders who monitor corporate responsibility internationally. Negotiation techniques for professionals responsibly doing business abroad are presented.

Cases

Twenty-three cases are included in this edition, fourteen of which are new and three thoroughly updated.

Chapter 1

1. Bernard L. Madoff Investment Securities LLC: Wall Street Trading Firm
2. Cyberbullying: Who's to Blame and What Can Be Done?

Chapter 2

3. Ford's Pinto Fires: The Retrospective View of Ford's Field Recall Coordinator

4. Jerome Kerviel: Rogue Trader or Misguided Employee? What Really Happened at the Société Générale?
5. Samuel Waksal at ImClone

Chapter 3

6. The BP *Deepwater Horizon* Explosion and Oil Spill: Crisis and Aftermath
7. Mattel Toy Recalls
8. Genetic Discrimination

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14. Neuromarketing
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17. Kaiser Permanente: A Crisis of Communication, Values, and Systems Failure
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Chapter 8

21. Google in China: Still "Doing No Evil"?
22. Sweatshops: Not Only a Global Issue
23. The U.S. Industrial Food System

Acknowledgments

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Joseph W. Weiss
Bentley University

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Case Authorship

Editing help was provided by Laura Gray, Lu Bai, and Matt Zamorski.

Case 1 Bernard L. Madoff Investment Securities LLC: Wall Street Trading Firm

Alba Skurti, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 2 Cyberbullying: Who's to Blame and What Can Be Done?

Roseleen Dello Russo and Lauren Westling, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 3 Ford's Pinto Fires: The Retrospective View of Ford's Field Recall Coordinator

Dennis A. Gioia, Professor of Organizational Behavior, Smeal College of Business, Pennsylvania State University, provided the personal reflections in this case. Michael K. McCuddy, Valparaiso University, provided background information and discussion questions.

Case 4 Jerome Kerviel: Rogue Trader or Misguided Employee? What Really Happened at the Société Générale?

Steve D'Aquila, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 5 Samuel Waksal at ImClone

Amy Vensku, MBA Bentley student under the direction of Professor Joseph W. Weiss, and edited and adapted for this text by Michael K. McCuddy, Valparaiso University and Matt Zamorski, Bentley University.

Case 6 The BP *Deepwater Horizon* Explosion and Oil Spill: Crisis and Aftermath

Jill Stonehouse and Bianlbahen Patel, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 7 Mattel Toy Recalls

Mike Ladd, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 8 Genetic Discrimination

Jaclyn Publicover, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 9 Conscious Capitalism: What Is It? Why Do We Need It? Does It Work?

John Warden, Bentley University, edited by Professor Joseph W. Weiss.

Case 10 Goldman Sachs: Hedging a Bet and Defrauding Investors

Dean Koutris and Jess Sheynman, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 11 Google Books

Steve D'Aquila, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 12 For-Profit Universities: Opportunities, Issues, and Promises

Alicia Cabrera and Nate Pullen, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 13 Fracking: Drilling for Disaster?

Lauren Casas and Ned Coffee, MBA Bentley students, under the direction of Professor Joseph W. Weiss, Bentley University, with editorial revisions made by Laura Gray, Matt Zamorski, and Lu Bai.

Case 14 Neuromarketing

Eddy Fitzgerald and Jennifer Johnson, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 15 Wal-Mart: Challenges with Gender Discrimination

Michael K. McCuddy, the Louis S. and Mary L. Morgal Chair of Christian Business Ethics and Professor of Management, College of Business Administration, Valparaiso University.

Case 16 Vioxx, Dodge Ball: Did Merck Try to Avoid the Truth?

Sean Downey, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 17 Kaiser Permanente: A Crisis of Communication, Values, and Systems Failure

Sarah O'Neill, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 18 Social Networking and Social Responsibility

Adam Schilke, Kimberly Benevides, and Eden Kyne, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 19 Preemployment Screening and Facebook: Ethical Considerations

Carl Forziati, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

Case 20 Women on Wall Street: Fighting for Equality in a Male-Dominated Industry

Monica Meunier, under the direction of Professor Joseph W. Weiss, and adapted and edited for this text by Michael K. McCuddy, Valparaiso University.

Case 21 Google in China: Still "Doing No Evil"?

Professor Joseph W. Weiss, Bentley University, edited by Lu Bai.

Case 22 Sweatshops: Not Only a Global Issue

Michael K. McCuddy, the Louis S. and Mary L. Morgal Chair of Christian Business Ethics and Professor of Management, College of Business Administration, Valparaiso University.

Case 23 The U.S. Industrial Food System

Brenda Pasquarello, Bentley University, under the direction of Professor Joseph W. Weiss, Bentley University.

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1

BUSINESS ETHICS, THE CHANGING ENVIRONMENT, AND STAKEHOLDER MANAGEMENT

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OPENING CASE

> Blogger: "Hi. i download music and movies, limewire and torrent. is it illegal for me to download or is it just illegal for the person uploading it. does anyone know someone who was caught and got into trouble for it, what happened them. Personally I dont see a difference between downloading a song or taping it on a cassette from a radio!!"[1]

The Recording Industry Association of America (RIAA), on behalf of its member companies and copyright owners, has sued more than 30,000 people for unlawful downloading. RIAA detectives log on to peer-to-peer networks where they easily identify illegal activity since users' shared folders are visible to all. The majority of these cases have been settled out of court for $1,000–$3,000, but fines per music track can go up to $150,000 under the Copyright Act.

The nation's first file-sharing defendant to challenge an RIAA lawsuit, Jammie Thomas-Rasset, reached the end of the appeals process to

overturn a jury-determined $222,000 fine in 2013. She was ordered to pay this amount, which she argued was unconstitutionally excessive, for downloading and sharing 24 copyrighted songs using the now-defunct file-sharing service Kazaa. The Supreme Court has not yet heard a file-sharing case, having also declined without comment to review the only other appeal following Thomas-Rasset's. (In that case, the Court let stand a federal jury-imposed fine of $675,000 against Joel Tenenbaum for downloading and sharing 30 songs.) "As I've said from the beginning, I do not have now, nor do I anticipate in the future, having $220,000 to pay this," Thomas-Rasset said. "If they do decide to try and collect, I will file for bankruptcy as I have no other option."[2]

Students often use university networks to illegally distribute copyrighted sound recordings on unauthorized peer-to-peer services. The RIAA has issued subpoenas to universities nationwide, including networks in Connecticut, Georgia, Kansas, Michigan, Minnesota, New Jersey, Pennsylvania, Rhode Island, Texas, Virginia, and Washington. Most universities give up students' identities only after offering an opportunity to stop the subpoena with their own funds. As in earlier rounds of lawsuits, the RIAA is utilizing the "John Doe" litigation process, which is used to sue defendants whose names are not known.

RIAA president Cary Sherman has discussed the ongoing effort to reach out to the university community with proactive solutions to the problem of illegal file-sharing on college campuses: "It remains as important as ever that we continue to work with the university community in a way that is respectful of the law as well as university values. That is one of our top priorities, and we believe our constructive outreach has been enormously productive so far. Along with offering students legitimate music services, campus-wide educational and technological initiatives are playing a critical role. But there is also a complementary need for enforcement by copyright owners against the serious offenders—to remind people that this activity is illegal."

He added: "Illegally downloading music from the Internet costs everyone—the musicians not getting compensated for their craft, the owners and employees of the thousands of record stores that have been forced to close, legitimate online music services building their businesses, and consumers who play by the rules and purchase their music legally."

On the other hand, once the well-funded RIAA initiates a lawsuit, many defendants are pressured to settle out of court in order to avoid oppressive legal expenses. Others simply can't take the risk of large fines that juries have shown themselves willing to impose.

New technologies and the trend toward digital consumption have made intellectual property both more critical to businesses' bottom lines and more difficult to protect. No company, big or small, is immune to the intellectual property protection challenge. Illegal downloads of

music are not the only concern. A new wave of lawsuits is being filed against individuals who illegally download movies through sites like Napster and BitTorrent. In 2011, the U.S. Copyright Group initiated "the largest illegal downloading case in US history" at the time, suing over 23,000 file sharers who illegally downloaded Sylvester Stallone's movie *The Expendables.* This case was expanded to include the 25,000 users who also downloaded Voltage Pictures' *The Hurt Locker,* which increased the total number of defendants to approximately 50,000, all of whom used peer-to-peer downloading through BitTorrent. The lawsuits were filed based on the illegal downloads made from an Internet Protocol (IP) address. The use of an IP address as identifier presents ethical issues–for example, should a parent be responsible for a child downloading a movie through the family's IP address? What about a landlord who supplied Internet to a tenant?

Digital books are also now in play. In 2012, a lawsuit was filed in China against technology giant Apple for sales of illegal book downloads through its App Store. Nine Chinese authors are demanding payment of $1.88 million for unauthorized versions of their books that were submitted to the App Store and sold to consumers for a profit. Again, the individual IP addresses are the primary way of determining who performed the illegal download. Telecom providers and their customers face privacy concerns, as companies are being asked for the names of customers associated with IP addresses identified with certain downloads.

Privacy activists argue that an IP address (which identifies the subscriber but not the person operating the computer) is private, protected information that can be shown during criminal but not civil investigations. Fred von Lohmann, senior staff attorney with the Electronic Frontier Foundation, has suggested on his organization's blog that "courts are not prepared to simply award default judgments worth tens of thousands of dollars against individuals based on a piece of paper backed by no evidence."[3]

1.1 Business Ethics and the Changing Environment

The Internet is changing everything: the way we communicate, relate, read, shop, bank, study, listen to music, get news and "TV," and participate in politics. Of course the last "third billion" of people in undeveloped countries are not participating on broadband as is the rest of the world,[4] but they predictably will, first through mobile phones. Businesses and governments operate in and are disrupted by changing technological, legal, economic, social, and political environments with competing stakeholders and power claims, as many Middle Eastern countries in particular are experiencing. Also, as this chapter's opening case shows, there is more than one side to every complex issue and debate involving businesses, consumers, families, other institutions, and professionals.

When stakeholders and companies cannot agree or negotiate competing claims among themselves, the issues generally go to the courts.

The RIAA, in the opening case, does not wish to alienate too many college students because they are also the music industry's best customers. At the same time, the association believes it must protect those groups it represents. Not all stakeholders in this controversy agree on goals and strategies. For example, not all music artists oppose students downloading or even sharing some of their copyrighted songs. Offering free access to some songs is a good advertising tactic. On the other hand, shouldn't those songwriters and recording companies who spend their time and money creating, marketing, distributing, and selling their intellectual property protect that property? Is file sharing, without limits or boundaries, stealing other people's property? If not, what is this practice to be called? If file sharing continues in some form, and ends up helping sales for many artists, will it become legitimate? Should it? Is this just the new way business models are being changed by 15–26 year olds? While the debate continues, individuals (15 year olds and younger in many cases) who still illegally share files have rights as private citizens under the law, and recording companies have rights of property protection. Who is right and who is wrong, especially when two rights collide? Who stands to lose and who to gain? Who gets hurt by these transactions? Which group's ethical positions are most defensible?

Stakeholders are individuals, companies, groups, and even governments and their subsystems that cause and respond to external issues, opportunities, and threats. Corporate scandals, globalization, deregulation, mergers, technology, and global terrorism have accelerated the rate of change and brought about a climate of uncertainty in which stakeholders must make business and moral decisions. Issues concerning questionable ethical and illegal business practices confront everyone, as the following examples illustrate:

- The subprime lending crisis in 2008 involved stakeholders as varied as consumers, banks, mortgage companies, real estate firms, and homeowners. Many companies that sold mortgages to unqualified buyers lied about low-risk, high-return products. Wall Street companies, while thriving, are also settling lawsuits stemming from the 2008 crisis. In 2013, "Hundreds of thousands of subprime borrowers are still struggling. Subprime securities still pose a significant legal risk to the firms that packaged them, and they use up capital that could be deployed elsewhere in the economy."[5] In 2011, Bank of America announced that it would "take a whopping $20 billion hit to put the fallout from the subprime bust behind it and satisfy claims from angry investors."[6] The ethics and decisions precipitating the crisis contributed to tilting the U.S. economy toward recession, with long-lasting effects.
- The corporate scandals in the 1990s through 2001 at Enron, Adelphia, Halliburton, MCI WorldCom, Tyco, Arthur Andersen, Global Crossing, Dynegy, Qwest, Merrill Lynch, and other firms that once jarred shareholder and public confidence in Wall Street and corporate governance may now seem like ancient history to those with short-term memories. Enron's

bankruptcy with assets of $63.4 billion defies imagination, but WorldCom's bankruptcy set the record for the largest corporate bankruptcy in U.S. history (Benston, 2003). Only 22% of Americans express a great deal or quite a lot of confidence in big business, compared to 65% who express confidence in small business.[7] Confidence in big business reached its highest point in 1974 at 34%, and even during the dot-com boom in the late 1990s it hovered at 30%. The lowest rating of 16% was polled in 2009 after the subprime lending crisis, and although public confidence has slightly increased, the significant differential in American confidence between big and small business belies a public mistrust of big business that may not be easily repaired.[8]

- The debate continues over excessive pay to those chief executive officers (CEOs) who posted poor corporate performance. Large bonuses paid out during the financial crisis made executive pay a controversial topic, yet investors did little to solve the issue. "Investors had the opportunity to provide advisory votes on executive pay at financial firms that received TARP funds in 2009, and they gave thumbs up to pay packages at every single one of those institutions. This proxy season, with advisory votes now widely available (thanks to the Dodd-Frank Act), only five companies' executive compensation packages have received a thumbs down from shareholders."[9] The Bureau of Labor Statistics noted that while median CEO salaries grew at 27% in 2010, overall worker pay only increased by 2.1%. "It's been almost three years since Congress directed the Securities and Exchange Commission to require public companies to disclose the ratio of their chief executive officers' compensation to the median of the rest of their employees'. The agency has yet to produce a rule."[10] An independent 2013 analysis by Bloomberg showed that "Across the Standard & Poor's 500 Index of companies, the average multiple of CEO compensation to that of rank-and-file workers is 204, up 20 percent since 2009."[11]

- Some critics on the right of the political spectrum argue that companies are becoming overregulated since the scandals. Others argue there is not sufficient regulation of the largest financial companies. The Sarbanes-Oxley Act of 2002 is one response to those scandals. This act states that corporate officers will serve prison time and pay large fines if they are found guilty of fraudulent financial reporting and of deceiving shareholders. Implementing this legislation requires companies to create accounting oversight boards, establish ethics codes, show financial reports in greater detail to investors, and have the CEO and chief financial officer (CFO) personally sign off on and take responsibility for all financial statements and internal controls. Implementing these provisions is costly for corporations. Some claim their profits and global competitiveness are negatively affected and the regulations are "unenforceable."[12]

- U.S. firms are outsourcing work to other countries to cut costs and improve profits, work that some argue could be accomplished in the United States. Estimates of U.S. jobs outsourced range from 104,000 in 2000 to

400,000 in 2004, and to a projected 3.3 million by 2015. "Forrester Research estimated that 3.3 million U.S. jobs and about $136 billion in wages would be moved to overseas countries such as India, China, and Russia by 2015. Deloitte Consulting reported that 2 million jobs would move from the United States and Europe to overseas destinations within the financial services business. Across all industries the emigration of service jobs can be as high as 4 million."[13] Do U.S. employees who are laid off and displaced need protection, or is this practice part of another societal business transformation? Is the United States becoming part of a global supply chain in which outsourcing is "business as usual" in a "flat world," or is the working middle class in the United States and elsewhere at risk of predatory industrial practices and ineffective government polices?[14]

- Will robots, robotics, and artificial intelligence (AI) applications replace humans in the workplace? This interesting but disruptive development poses concerns. "The outsourcing of human jobs as a side effect of globalization has arguably contributed to the current unemployment crisis. However, a growing trend sees humans done away with altogether, even in the low-wage countries where many American jobs have landed".[15] What will be the ethical implications of the next wave of AI development, "where full-blown autonomous self-learning systems take us into the realm of science fiction—delivery systems and self-driving vehicles alone could change day-to-day life as we know it, not to mention the social implications."[16] AI also extends into electronic warfare (drones), education (robot assisted or led), and manufacturing (a Taiwanese company replaced a "human force of 1.2 million people with 1 million robots to make laptops, mobile devices and other electronics hardware for Apple, Hewlett-Packard, Dell and Sony").[17] One futurist predicted that as many as 50 million jobs could be lost to machines by 2030, and even 50% of all human jobs by 2040.

These large macro-level issues underlie many ethical dilemmas that affect business and individual decisions among stakeholders in organizations, professions, as well as individual lives. Before discussing stakeholder theory, and the management approach that it is based on, and how these perspectives and methods can help individuals and companies better understand how to make more socially responsible decisions, we take a brief look at the broader environmental forces that affect industries, organizations, and individuals.

Seeing the "Big Picture"

Pulitzer Prize-winning journalist Thomas Friedman, continues to track megachanges on a global scale. His 2011 book, *That Used to Be Us: How America Fell Behind in the World It Invented and How We Can Come Back,* suggests an agenda for change to meet larger challenges. His books, *The World Is Flat 3.0*, and *The Lexus and the Olive Tree*, vividly illustrate a macroenvironmental perspective that provides helpful insights into stakeholder and issues management mind-sets and approaches.[18] Friedman notes, "Like everyone

else trying to adjust to this new globalization system and bring it into focus, I had to retrain myself and develop new lenses to see it. Today, more than ever, the traditional boundaries between politics, culture, technology, finance, national security, and ecology are disappearing. You often cannot explain one without referring to the others, and you cannot explain the whole without reference to them all. I wish I could say I understood all this when I began my career, but I didn't. I came to this approach entirely by accident, as successive changes in my career kept forcing me to add one more lens on top of another, just to survive."[19]

After quoting Murray Gell-Mann, the Nobel laureate and former professor of theoretical physics at Caltech, Friedman continues, "We need a corpus of people who consider that it is important to take a serious and professional look at the whole system. It has to be a crude look, because you will never master every part or every interconnection. Unfortunately, in a great many places in our society, including academia and most bureaucracies, prestige accrues principally to those who study carefully some [narrow] aspect of a problem, a trade, a technology, or a culture, while discussion of the big picture is relegated to cocktail party conversation. That is crazy. We have to learn not only to have specialists but also people whose specialty is to spot the strong interactions and entanglements of the different dimensions, and then take a crude look at the whole."[20]

POINT/COUNTERPOINT

File Sharing: Harmful Theft or Sign of the Times?

This exercise provides a more complete case with student interaction.

> "I watch some of my favorite shows on hulu.com for free and I buy others on Amazon or iTunes. I pay a fee to use Pandora for ad-free internet radio, or Spotify for specific music playlists. But like many of my friends, I don't own a TV, so when there is no other way to access a show, I will download it from a torrent [file-sharing] site."
> —*Interview with a Generation Y "Millennial"*

The Recording Industry Association of America (RIAA), on behalf of its member companies and copyright owners, has sued more than 30,000 people for unlawful downloading. RIAA detectives log on to peer-to-peer networks where they easily identify illegal activity since users' shared folders are visible to all. The majority of these cases have been settled out of court for $1,000–$3,000, but fines per music track can go up to $150,000 under the Copyright Act.

The nation's first file-sharing defendant to challenge an RIAA lawsuit, Jammie Thomas-Rasset, in 2013 reached the end of the appeals process to overturn a jury-determined $222,000 fine. She was ordered to pay this amount, which she argued was unconstitutionally excessive, for downloading and sharing 24 copyrighted songs using the now-defunct file-sharing service Kazaa. The Supreme Court has not yet heard a file-sharing case, having also declined without comment to review the only other appeal following Thomas-Rasset's.

Students often use university networks to illegally distribute copyrighted sound recordings on unauthorized peer-to-peer services. The RIAA issues subpoenas to universities nationwide, including networks in Connecticut, Georgia, Kansas, Michigan, Minnesota, New Jersey, Pennsylvania, Rhode Island, Texas, Virginia, and Washington. Most universities give up students' identities only after offering an opportunity to stop the subpoena with their own funds. As in earlier rounds of lawsuits, the RIAA is utilizing the "John Doe" litigation process, which is used to sue defendants whose names are not known.

RIAA President Cary Sherman cites the ongoing effort to reach out to the university community with proactive solutions to the problem of illegal file sharing on college campuses, saying, "It remains as important as ever that we continue to work with the university community in a way that is respectful of the law as well as university values. . . . Along with offering students legitimate music services, campus-wide educational and technological initiatives are playing a critical role. But there is also a complementary need for enforcement by copyright owners against the serious offenders—to remind people that this activity is illegal and . . . costs everyone."

On the other hand, once the well-funded RIAA initiates a lawsuit, many defendants are pressured to settle out of court in order to avoid oppressive legal expenses. Others simply can't take the risk of large fines that juries have shown themselves willing to impose.

New technologies and the trend toward digital consumption have made intellectual property both more critical to businesses' bottom line and more difficult to protect. No company, big or small, is immune to the IP protection challenge. Illegal downloads of music are not the only concern. A new wave of lawsuits is being filed against individuals who illegally download movies through sites like Napster and BitTorrent.

In 2011, the U.S. Copyright Group initiated "the largest illegal downloading case in U.S. history" at the time, suing over 23,000 file sharers who illegally downloaded Sylvester Stallone's movie, *The Expendables*. This case was expanded to include the 25,000 users who also downloaded Voltage Pictures' *The Hurt Locker,* which increased the total number of defendants to approximately 50,000 who used peer-to-peer downloading through BitTorrent. The lawsuits are filed based on the illegal downloads made from an IP address.

Digital books are also now in play. In 2012, a lawsuit was filed in China against technology giant Apple for sales of illegal book downloads through the App Store. Nine Chinese authors are demanding payment of $1.88 million for unauthorized versions of their books that were submitted to the App Store and sold to consumers for a profit. Again, the individual IP addresses are the primary way of determining who performed the illegal download. Telecom providers and their customers face privacy concerns, as companies are being asked for the names of customers associated with IP addresses identified with certain downloads.

Privacy activists argue that an IP address (which identifies the subscriber but not the person operating the computer) is private, protected information

that can be shown during criminal but not civil investigations. Fred von Lohmann, senior staff attorney with the Electronic Frontier Foundation, has suggested on his organization's blog that "courts are not prepared to simply award default judgments worth tens of thousands of dollars against individuals based on a piece of paper backed by no evidence."

Instructions: (1) Each student team individually adopts *either* the Point *or* CounterPoint argument and justifies their reasons (arguments using this case and other evidence/opinions). (2) Then, either in teams or designated arrangements, each shares their reasons. (3) The class is debriefed and insights shared.

POINT: File sharing is theft, and endangers the entire structure of incentives that allows the creation of digital media. Downloading even one song illegally has severe costs for the musicians and the owners and employees of the companies that produce songs, and legitimate online music services, not to mention consumers who purchase music legally. Those responsible, even peripherally, for illegal file sharing should be tracked down by any means possible and held accountable for these costs and damages.

COUNTERPOINT: The generation that grew up with the advent of digital media has a well-cultivated expectation of ease and freedom when it comes to accessing music, television, and books using the Internet. Companies are willing to capitalize on that ease to boost their profits. It is unethical to use technology and the legal system to "make examples" of those (possibly innocent bystanders whose IP addresses were used by others) who are simply showing the flaws and gaps in distribution strategies.

SOURCES

The exercise was authored by Taya Weiss and draws on the following sources:

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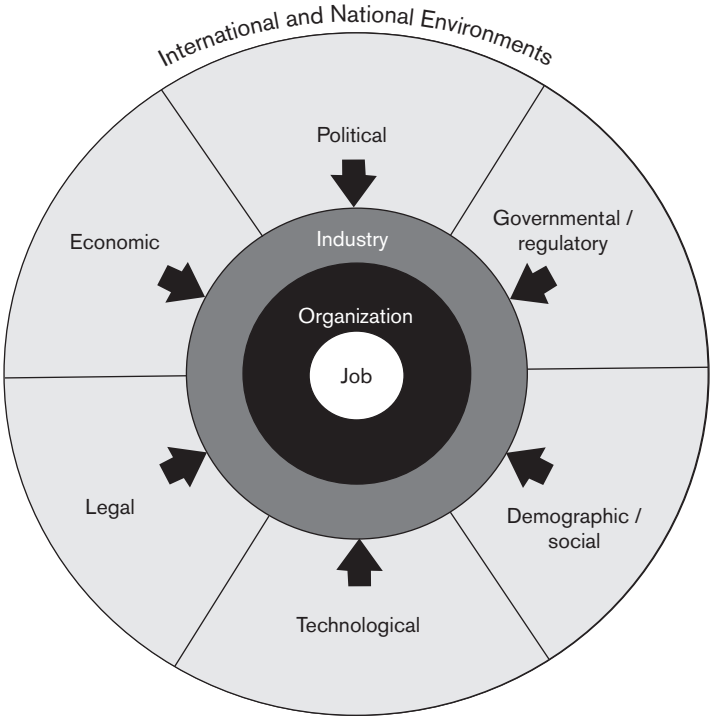
Environmental Forces and Stakeholders

Organizations and individuals are embedded in and interact with multiple changing local, national, and international environments, as the above discussion illustrates. These environments are increasingly merging into a global system of dynamically interrelated interactions among businesses and economies. We must "think globally before acting locally" in many situations. The macro-level environmental forces shown in Figure 1.1 affect the performance and operation of industries, organizations, and jobs. This framework can be

Figure 1.1

Environmental Dimensions Affecting Industries, Organizations, and Jobs



used as a starting point to identify trends, issues, opportunities, and ethical problems that affect people and stakes in different levels. A first step toward understanding stakeholder issues is to gain an understanding of environmental forces that influence stakes. As we present an overview of these environmental forces here, think of the effects and pressures each of the forces has on you.

The economic environment continues to evolve into a more global context of trade, markets, and resource flows. Large and small U.S. companies are expanding businesses and products overseas. Stock and bond market volatility and interdependencies across international regions are unprecedented, including the European market and the future of the euro, which is challenged by some defaulting economies. The rise of China and India presents new trade opportunities and business practices, if human rights problems can be solved in those countries. Do you see your career and next job being affected by this round of globalization?

The technological environment has ushered in the advent of electronic communication, online social networking, and near-constant connectivity to the Internet, all of which are changing economies, industries, companies, and jobs. U.S. jobs that are based on routine technologies and rules-oriented procedures are vulnerable to outsourcing. Online technologies facilitate changing corporate "best practices." Company supply chains are also becoming virtually and globally integrated online. Although speed, scope, economy of scale, and efficiency are transforming transactions through information technology, privacy and surveillance issues continue to emerge. The boundary between surveillance and convenience also continues to blur. Has the company or organization for which you work used surveillance to monitor Internet use?

Electronic democracy is changing the way individuals and groups think and act on political issues. Instant web surveys broadcast over interactive web sites have created a global chat room for political issues. Creation of online communities in the 2004, 2008, and 2012 presidential campaigns have proved an effective political strategy for both U.S. parties' fundraising programs and mobilizing of new voters. Have you used the Internet to participate in a national, local, or regional political process?

The government and legal environments continue to create regulatory laws and procedures to protect consumers and restrict unfair corporate practices. Since Enron and other corporate scandals, the Sarbanes-Oxley Act of 2002 and the revised 2004 Federal Sentencing Guidelines were created to audit and constrain corporate executives from blatant fraudulence on financial statements. The Dodd-Frank Act of 2010 established the Consumer Financial Protection Bureau, whose mission is to protect consumers by carrying out federal consumer financial laws, educating consumers, and hearing complaints from the public, and more recently that Bureau has been functioning to help citizens with credit card abuses in particular.[21]

Several federal agencies are also changing—or ignoring—standards for corporations. The U.S. Food and Drug Administration (FDA), for example, has sped up the required market approval time for new drugs sought by

patients with life-threatening diseases, but lags behind in taking some unsafe drugs off the market.

Uneven regulation of fraudulent and anticompetitive practices affects competition, shareholders, and consumers. Executives from Enron and other large U.S. firms involved in scandals have been tried and sentenced. Should the banks that loaned them funds also be charged with wrongdoing? Should U.S. laws be enforced more evenly? Who regulates the regulators? The subprime lending crisis raises some of the same questions. Who can the public trust for advice about mortgages and substantial loans? Who is responsible and accountable for educating and constraining the public in such transactions in a democratic, capitalist society?

Legal questions and issues affect all of these environmental dimensions and every stakeholder and investor. How much power should the government have to administer laws to protect citizens and ensure that business transactions are fair? Also, who protects the consumer in a free-market system? These issues, which are exemplified in the file-sharing controversy as summarized in this chapter's opening case, question the nature and limits of consumer and corporate laws in a free-market economy.

The demographic and social environment continues to change as national boundaries experience the effects of globalization and the workforce becomes more diverse. Employers and employees are faced with aging and very young populations; minorities becoming majorities; generational differences; and the effects of downsizing and outsourcing on morale, productivity, and security. How can companies effectively integrate a workforce that is increasingly both younger and older, less educated and more educated, technologically sophisticated and technologically unskilled?

In this book these environmental factors are incorporated into a stakeholder and issues management approach that also includes an ethical analysis of actors external and internal to organizations. The larger perspective underlying these analytical approaches is represented by the following question: How can the common good of all stakeholders in controversial situations be realized?

Stakeholder Management Approach

How do companies, the media, political groups, consumers, employees, competitors, and other groups respond in socially ethical and responsible ways when they effect and are affected by an issue, dilemma, threat, or opportunity from the environments just described? The stakeholder theory expands a narrow view of corporations from a stockholder-only perspective to include the many stakeholders who are also involved in how corporations envision the future, treat people and the environment, and serve the common good for the many. Implementing this view starts with understanding the ethical imperatives and moral understandings that corporations that use natural resources and the environment must serve, as well as providing for those who buy their products and services. This view and accompanying methods are explained in more detail in Chapters 2 and 3 especially and inform the whole text.

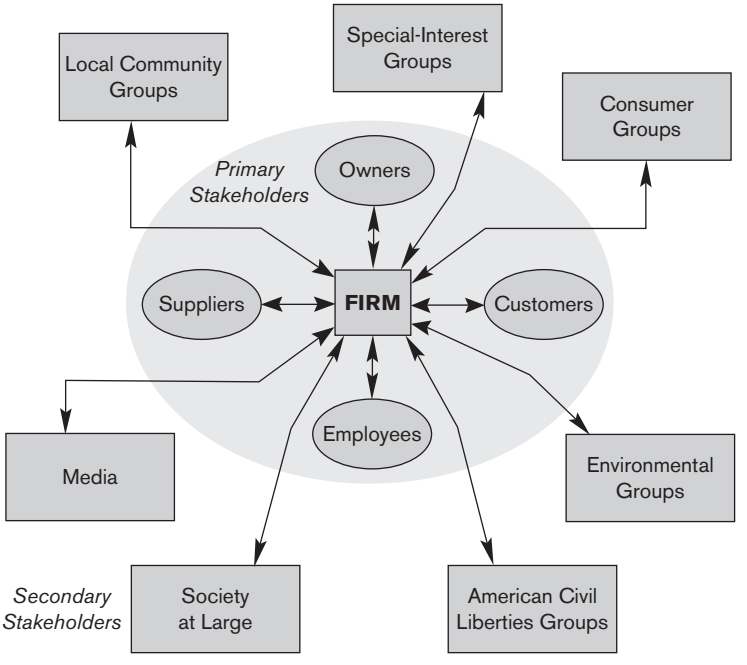
The stakeholder theory begins to address these questions by enabling individuals and groups to articulate collaborative, win–win strategies based on:

1. Identifying and prioritizing issues, threats, or opportunities.
2. Mapping who the stakeholders are.
3. Identifying their stakes, interests, and power sources.
4. Showing who the members of coalitions are or may become.
5. Showing what each stakeholder's ethics are (and should be).
6. Developing collaborative strategies and dialogue from a "higher ground" perspective to move plans and interactions to the desired closure for all parties.

Chapter 3 lays out specific steps and strategies for analyzing stakeholders. Here, our aim is to develop awareness of the ethical and social responsibilities of different stakeholders. As Figure 1.2 illustrates, there can be a wide range of stakeholders in any situation. We turn to a general discussion of "business ethics" in the following section to introduce the subject and motivate you to investigate ethical dimensions of organizational and professional behavior.

Figure 1.2

Primary vs. Secondary Stakeholder Groups



1.2 What Is Business Ethics? Why Does It Matter?

Business ethicists ask, "What is right and wrong, good and bad, harmful and beneficial regarding decisions and actions in organizational transactions?" Ethical reasoning and logic is explained in more detail in Chapter 2, but we note here that approaching problems using a moral frame of reference can influence solution paths as well as options and outcomes. Since "solutions" to business and organizational problems may have more than one alternative, and sometimes no right solution may seem available, using principled ethical thinking provides structured and systematic ways of decision making based on values, not only perceptions that may be distorted, pressures from others, or the quickest and easiest available options—that may prove more harmful.

What Is Ethics and What Are the Areas of Ethical Theory?

Ethics derives from the Greek word *ethos*—meaning "character"—and is also known as moral philosophy, which is a branch of philosophy that involves "systematizing, defending and recommending concepts of right and wrong conduct."[22] Ethics involves understanding the differences between right and wrong thinking and actions, and using principled decision making to choose actions that do not hurt others. Although intuition and creativity are often involved in having to decide between what seems like two "wrong" or less desirable choices in a dilemma where there are no easy alternatives, using ethical principles to inform our thinking before acting hastily may reduce the negative consequences of our actions. Classic ethical principles are presented in more detail in the next chapter, but by way of an introduction, the following three general areas constitute a framework for understanding ethical theories: metaethics, normative ethics, and descriptive ethics.[23]

Metaethics considers where one's ethical principles "come from, and what they mean." Do one's ethical beliefs come from what society has prescribed? Did our parents, family, religious institutions influence and shape our ethical beliefs? Are our principles part of our emotions and attitudes? Metaethical perspectives address these questions and focus on issues of universal truths, the will of God, the role of reason in ethical judgments, and the meaning of ethical terms themselves.[24] More practically, if we are studying a case or observing an event in the news, we can inquire about what and where a particular CEO's or professional's ethical principles (or lack thereof) are and where in his/her life and work history these beliefs were adopted.

Normative ethics is more practical; this type of ethics involves prescribing and evaluating ethical behaviors—what should be done in the future. We can inquire about specific moral standards that govern and influence right from wrong conduct and behaviors. Normative ethics also deals with what habits we need to develop, what duties and responsibilities we should follow, and the consequences of our behavior and its effects on others. Again, in a business or organizational context, we observe and address ethical problems and issues with individuals, teams, leaders and address ways of preventing and/or solving ethical dilemmas and problems.

Descriptive ethics involves the examination of other people's beliefs and principles. It also relates to presenting—describing but not interpreting or evaluating—facts, events, and ethical actions in specific situations and places. In any context—organizational, relationship, or business—our aim here is to understand, not predict, judge, or solve an ethical or unethical behavior or action.

Learning to think, reason, and act ethically helps us to become aware of and recognize potential ethical problems. Then we can evaluate values, assumptions, and judgments regarding the problem *before* we act. Ultimately, ethical principles alone cannot answer what the late theologian Paul Tillich called "the courage to be" in serious ethical dilemmas or crises. We can also learn from business case studies, role playing, and discussions on how our actions affect others in different situations. Acting accountably and responsibly is still a choice.

Laura Nash defined business ethics as "the study of how personal moral norms apply to the activities and goals of commercial enterprise. It is not a separate moral standard, but the study of how the business context poses its own unique problems for the moral person who acts as an agent of this system." Nash stated that business ethics deals with three basic areas of managerial decision making: (1) choices about what the laws should be and whether to follow them; (2) choices about economic and social issues outside the domain of law; and (3) choices about the priority of self-interest over the company's interests.[25]

Unethical Business Practices and Employees

The seventh (2011) National Business Ethics Survey (NBES), which obtained 4,800 responses representative of the entire U.S. workforce,[26] reported an ethical environment unlike any we have seen before in America: "American employees are doing the right thing more than ever before, but in other ways employees' experiences are worse than in the past."[27] The survey findings are summarized below in terms of the "bad" and "good" news found in the workforce:

The "Bad" News

- Retaliation is on the rise against employee whistle-blowers, with 22% of employees who reported misconduct experiencing some form of retaliation.
- More employees (13%) feel pressure to compromise their ethical standards in order to do their jobs.
- The number of companies with weak ethical cultures has grown to near-record highs, now at 42%.

The "Good" News

- The workplace is experiencing the lowest levels of misconduct, with only 45% of employees witnessing misconduct.
- A record high (65%) of those employees now report misconduct.

- Management is improving its oversight and increasing efforts to raise awareness about ethics—34% of employees felt more closely watched by management, and 42% of employees recognized increased ethical awareness efforts.

The authors of the survey note that an ethical downturn is on the horizon. The economic decline and high unemployment have created a unique ethical environment fueled by other modern factors like social networking. "Research has revealed a significant ethics divide between those who are active on social networks and those who are not."[28]

Specific Types of Ethical Misconduct Reported

The top five most frequently observed types of misconduct were: misuse of company time (33%), abusive behavior (21%), lying to employees (20%), company resource abuse (20%), and violating company Internet use policies (16%). Types of misconduct with the largest increases included: sexual harassment, substance abuse, insider trading, illegal political contributions, stealing, and environmental violations.[29]

Many employees still do not report misconduct that they observe, and fear of retaliation is increasingly valid. "When all employees are asked whether they could question management without fear of retaliation, 19 percent said it was not safe to do so." The most common forms of retaliation include: exclusion by management from decision and work activity (64%), cold shoulder attitudes from other employees (62%), verbal abuse from management (62%), not given promotions or raises (55%), and cut pay or hours (46%). This retaliation can lead to instability in the workplace by driving away talented employees. "About seven of 10 employees who experienced retaliation plan to leave their current place of employment within five years."[30]

Ethics and Compliance Programs

Ethical components of company culture include: "management's trustworthiness, whether managers at all levels talk about ethics and model appropriate behavior, the extent to which employees value and support ethical conduct, accountability and transparency." Eleven percent of companies in 2011 had weak ethical cultures. Companies can reduce ethics risks by investing in a strong ethics and compliance program: "86% of companies with a well-implemented ethics and compliance program also have a strong ethics culture."[31]

The Retaliation Trust/Fear/Reality Disconnect

Of the 65% of employees who reported witnessing misconduct in the 2011 NBES, 22% (or approximately 9 million employees) experienced retaliation. These victims of retaliation are far more likely to report misconduct to an outside source, rather than to a member of management. This can have many negative consequences for stakeholders involved.[32]

Reporting rates are much higher in companies that have well-implemented ethics *and* compliance programs; only 6% of employees in companies with strong ethics and compliance programs did not report observed misconduct.

It is interesting to note the impact of social networking on the ethical environment of a company. According to the 2011 NBES:

- "Active social networkers report far more negative experiences of workplace ethics. As a group, they are almost four times more likely to experience pressure to compromise standards and about three times more likely to experience retaliation for reporting misconduct than co-workers who are less active with social networking. They also are far more likely to observe misconduct." Seventy-two percent of active social networkers surveyed observed misconduct; 42% felt pressure to compromise standards; and 56% experienced retaliation after reporting misconduct.
- Active social networkers, as discussed in this chapter's opening case, are also more likely to believe that questionable behaviors are acceptable. Forty-two percent of active social networkers felt that it was acceptable to blog or tweet negatively about their company or colleagues; 42% felt that it was acceptable to buy personal items on a company credit card as long as it was paid back; 51% felt it was acceptable to do less work as payback for cuts in pay or benefits; 50% felt it was acceptable to keep a copy of confidential work documents in case you need them in your next job; and 46% felt that it was acceptable to take a copy of work software home for use on their personal computer. Only about 10% of non-active social networkers felt that these activities were acceptable.[33] Are you an active social networker? Do these results resonate with you?

These findings suggest that any useful definition of business ethics must address a range of problems in the workplace, including relationships among professionals at all levels and among corporate executives and external groups.

Why Does Ethics Matter in Business?

"Doing the right thing" matters to firms, taxpayers, employees, and other stakeholders, as well as to society. To companies and employers, acting legally and ethically means saving billions of dollars each year in lawsuits, settlements, and theft. One study found that the annual business costs of internal fraud range between the annual gross domestic profit (GDP) of Bulgaria ($50 billion) and that of Taiwan ($400 billion). It has also been estimated that theft costs companies $600 billion annually, and that 79% of workers admit to or think about stealing from their employers. Other studies have shown that corporations have paid significant financial penalties for acting unethically.[34] The U.S. Department of Commerce noted that "as many as one-third of all business failures annually can be attributed to employee theft." Experts have estimated that approximately 40% of fraud and theft losses to American businesses are internal.[35]

Relationships, Reputation, Morale, and Productivity

Costs to businesses also include deterioration of relationships; damage to reputation; declining employee productivity, creativity, and loyalty; ineffective information flow throughout the organization; and absenteeism. Companies that have a reputation for unethical and uncaring behavior toward employees also have a difficult time recruiting and retaining valued professionals.

Integrity, Culture, Communication, and the Common Good

Strong ethical leadership goes hand in hand with strong integrity. Both ethics and integrity have a significant impact on a company's operations. " 'History has often shown the importance of ethics in business – even a single lapse in judgment by one employee can significantly affect a company's reputation and its bottom line.' Leaders who show a solid moral compass and set a forthright example for their employees foster a work environment where integrity becomes a core value."[36] A study of the 50 best companies to work for in Canada (based on survey responses from over 100,000 Canadian employees at 115 organizations, with input from 1,400 leaders and human resources professionals) found that integrity and ethics matter in the following ways: there is more flexibility and balance; values have changed; and organizations are valuing new employees more since the demographics have changed.[37] These changes are explained next.

Integrity/Ethics

What is the degree to which coworkers, managers, and senior leaders display integrity and ethical conduct? Eighty-eight percent of employees at the top 10 best employers agreed or strongly agreed that coworkers displayed integrity and ethical conduct at all times, whereas only 60% felt that way at the bottom 10 organizations. With respect to managers, the numbers were 90% at the top 10 and 63% at the bottom 10 organizations. A bigger difference existed with regard to whether senior leadership displayed integrity and ethical conduct at all times, with 89% of employees at the top 10 best employers agreeing or strongly agreeing, whereas less than half—48%—felt that way at the bottom 10 employers.[38]

The same study found that "engagement is higher at organizations where employees feel they share the same values as their employer" and that "sense of 'common purpose' can increase employee commitment, especially amongst older workers." The authors also noted that "a perceived lack of integrity on the part of co-workers, managers and leaders has, as expected, a detrimental effect on engagement. What was perhaps unanticipated in the study findings, however, was the really negative opinion of the ethics of senior leadership at low-engagement organizations."

Working for the Best Companies

Employees care about ethics because they are attracted to ethically and socially responsible companies. *Fortune* magazine regularly publishes the 100 best com-

panies for which to work (http://money.cnn.com/magazines/fortune/best-companies).[39] Although the list continues to change, it is instructive to observe some of the characteristics of good employers that employees repeatedly cite. The most frequently mentioned characteristics include profit sharing, bonuses, and monetary awards. However, the list also contains policies and benefits that balance work and personal life and those that encourage social responsibility. Consider these policies described by employees:

- When it comes to flextime requests, managers are encouraged to "do what is right and human."
- There is an employee hotline to report violations of company values.
- Managers will fire clients who don't respect its security officers.
- Employees donated more than 28,000 hours of volunteer labor last year.

The public and consumers benefit from organizations acting in an ethically and socially responsible manner. Ethics matters in business because all stakeholders stand to gain when organizations, groups, and individuals seek to do the right thing, as well as to do things the right way. Ethical companies create investor loyalty, customer satisfaction, and business performance and profits.[40] The following section presents different levels on which ethical issues can occur.

1.3 Levels of Business Ethics

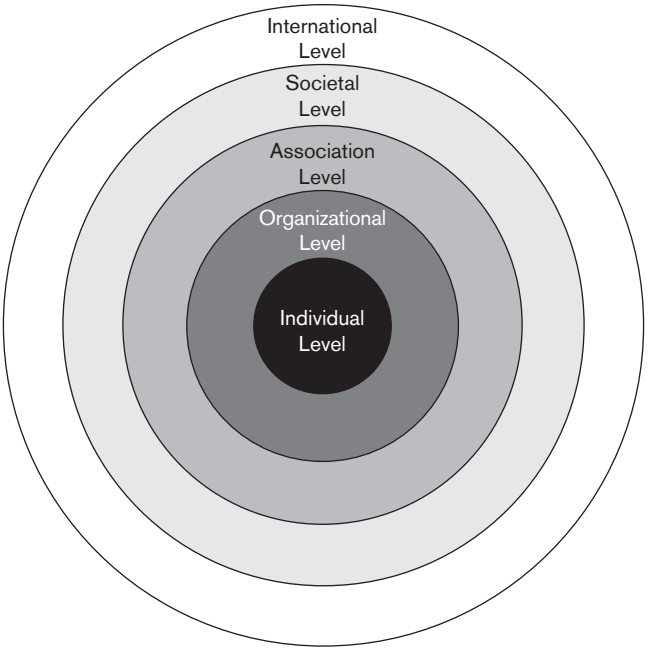
Because ethical problems are not only an individual or personal matter, it is helpful to see where issues originate, and how they change. Business leaders and professionals manage a wide range of stakeholders inside and outside their organizations. Understanding these stakeholders and their concerns will facilitate our understanding of the complex relationships between participants involved in solving ethical problems.

Ethical and moral issues in business can be examined on at least five levels. Figure 1.3 illustrates these five levels: individual, organizational, association, societal, and international.[41] Aaron Feuerstein's now classic story as former CEO of Malden Mills exemplifies how an ethical leader in his seventies turned a disaster into an opportunity. His actions reflected his person, faith, allegiance to his family and community, and sense of social responsibility.

On December 11, 1995, Malden Mills in Lawrence, Massachusetts—manufacturer of Polartec and Polarfleece fabrics and the largest employer in the city—was destroyed by fire. Over 1,400 people were out of work. Feuerstein stated, "Everything I did after the fire was in keeping with the ethical standards I've tried to maintain my entire life, so it's surprising we've gotten so much attention. Whether I deserve it or not, I guess I became a symbol of what the average worker would like corporate America to be in a time when the American dream has been pretty badly injured." Feuerstein announced shortly after the fire that the employees would stay on the payroll while the plant was rebuilt for 60 days. He noted, "I think it was a wise

Figure 1.3

Business Ethics Levels



Source: Carroll, Archie B. (1978). Linking business ethics to behavior in organizations. *SAM Advanced Management Journal, 43(3),* 7. Reprinted with permission from Society for Advancement of Management, Texas A&M University, College of Business.

business decision, but that isn't why I did it. I did it because it was the right thing to do."

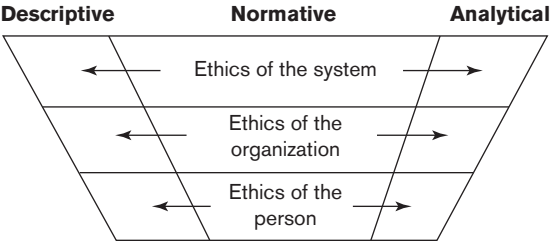
Feuerstein could have taken the $300 million in insurance and retired, or even offshored the entire operation. Instead, he paid out $25 million to his employees and rebuilt the plant. Feuerstein spent the insurance funds, borrowed $100 million more, and built a new plant that is both environmentally friendly and worker-friendly. It is also unionized. Feuerstein was invited to President Clinton's State of the Union address and serves as an icon in the business ethics and leadership community, regardless of the fate of Malden Mills going forward.[42]

Asking Key Questions

It is helpful to be aware of the ethical levels of a situation and the possible interaction between these levels when confronting a question that has moral implications. The following questions can be asked when a problematic decision or action is perceived (before it becomes an ethical dilemma):

Figure 1.4

A Framework for Classifying Ethical Issues and Levels



Source: Matthews, John B., Goodpaster, Kenneth E., and Laura L. Nash. (1985). *Policies and persons: A casebook in business ethics,* 509. New York: McGraw-Hill. Reproduced with permission from Kenneth E. Goodpaster.

- What are my core values and beliefs?
- What are the core values and beliefs of my organization?
- Whose values, beliefs, and interests may be at risk in this decision? Why?
- Who will be harmed or helped by my decision or by the decision of my organization?
- How will my own and my organization's core values and beliefs be affected or changed by this decision?
- How will I and my organization be affected by the decision?

Figure 1.4 offers a graphic to help identify the ethics of the system (i.e., a country or region's customs, values, and laws), your organization (i.e., the written formal and informal acceptable norms and ways of doing business), and your own ethics, values, and standards.

In the following section, popular myths about business ethics are presented to challenge misconceptions regarding the nature of ethics and business. You may take the "Quick Test of Your Ethical Beliefs" before reading this section.

Ethical Insight 1.1

Quick Test of Your Ethical Beliefs

Answer each question with your first reaction. Circle the number, from 1 to 4, that best represents your beliefs, if 1 represents "Completely agree," 2 represents "Often agree," 3 represents "Somewhat disagree," and 4 represents "Completely disagree."

1. I consider money to be the most important reason for working at a job or in an organization. 1 2 3 4
2. I would hide truthful information about someone or something at work to save my job. 1 2 3 4

3. Lying is usually necessary to succeed in business. 1 2 3 4
4. Cutthroat competition is part of getting ahead in the business world. 1 2 3 4
5. I would do what is needed to promote my own career in a company, short of committing a serious crime. 1 2 3 4
6. Acting ethically at home and with friends is not the same as acting ethically on the job. 1 2 3 4
7. Rules are for people who don't really want to make it to the top of a company. 1 2 3 4
8. I believe that the "Golden Rule" is that the person who has the gold rules. 1 2 3 4
9. Ethics should be taught at home and in the family, not in professional or higher education. 1 2 3 4
10. I consider myself the type of person who does whatever it takes to get a job done, period. 1 2 3 4

Add up all the points. Your Total Score is: _____

Total your scores by adding up the numbers you circled. The lower your score, the more questionable your ethical principles regarding business activities. The lowest possible score is 10, the highest 40. Be ready to give reasons for your answers in a class discussion.

1.4 Five Myths about Business Ethics

Not everyone agrees that ethics is a relevant subject for business education or dealings. Some have argued that "business ethics" is an oxymoron, or a contradiction in terms. Although this book does not advocate a particular ethical position or belief system, it argues that ethics is relevant to business transactions. However, certain myths persist about business ethics. The more popular myths are presented in Figure 1.5.

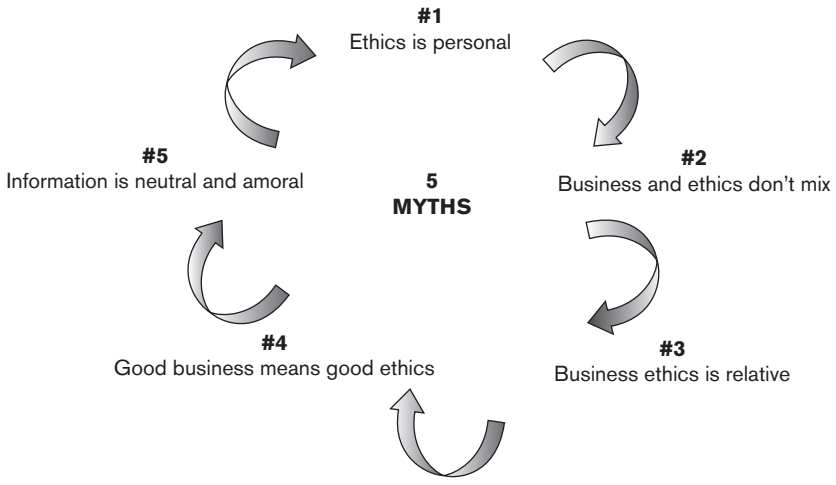
A myth is "a belief given uncritical acceptance by the members of a group, especially in support of existing or traditional practices and institutions."[43] Myths regarding the relationship between business and ethics do not represent truth but popular and unexamined notions. Which, if any, of the following myths have you accepted as unquestioned truth? Which do you reject? Do you know anyone who holds any of these myths as true?

Myth 1: Ethics Is a Personal, Individual Affair, Not a Public or Debatable Matter

This myth holds that individual ethics is based on personal or religious beliefs, and that one decides what is right and wrong in the privacy of one's conscience. This myth is supported in part by Milton Friedman, a well-known economist, who views "social responsibility," as an expression of business ethics, to be unsuitable for business professionals to address seriously or professionally because they are not equipped or trained to do so.[44]

Figure 1.5

Five Business Ethics Myths



Although it is true that individuals must make moral choices in life, including business affairs, it is also true that individuals do not operate in a vacuum. Individual ethical choices are most often influenced by discussions, conversations, and debates, and made in group contexts. Individuals often rely on organizations and groups for meaning, direction, and purpose. Moreover, individuals are integral parts of organizational cultures, which have standards to govern what is acceptable. Therefore, to argue that ethics related to business issues is mainly a matter of personal or individual choice is to underestimate the role organizations play in shaping and influencing members' attitudes and behaviors.

Studies indicate that organizations that act in socially irresponsible ways often pay penalties for unethical behavior.[45] In fact, the results of the studies advocate integrating ethics into the strategic management process because it is both the right and the profitable thing to do. Corporate social performance has been found to increase financial performance. One study notes that "analysis of corporate failures and disasters strongly suggests that incorporating ethics in before-profit decision making can improve strategy development and implementation and ultimately maximize corporate profits."[46] Moreover, the popularity of books, training, and articles on learning organizations and the habits of highly effective people among Fortune 500 and 1000 companies suggests that organizational leaders and professionals have a need for purposeful, socially responsible management training and practices.[47]

Myth 2: Business and Ethics Do Not Mix

This myth holds that business practices are basically amoral (not necessarily immoral) because businesses operate in a free market. This myth also asserts that management is based on scientific, rather than religious or ethical, principles.[48]

Although this myth may have thrived in an earlier industrializing U.S. society and even during the 1960s, it has eroded over the past two decades. The widespread consequences of computer hacking on individual, commercial, and government systems that affect the public's welfare, like identity theft on the Internet (stealing others' Social Security numbers and using their bank accounts and credit cards), and kickbacks, unsafe products, oil spills, toxic dumping, air and water pollution, and improper use of public funds have contributed to the erosion. The international and national infatuation with a purely scientific understanding of U.S. business practices, in particular, and of a value-free marketing system, has been undermined by these events. As one saying goes, "A little experience can inform a lot of theory."

The ethicist Richard DeGeorge has noted that the belief that business is amoral is a myth because it ignores the business involvement of all of us. Business is a human activity, not simply a scientific one, and, as such, can be evaluated from a moral perspective. If everyone in business acted amorally or immorally, as a pseudoscientific notion of business would suggest, businesses would collapse. Employees would openly steal from employers; employers would recklessly fire employees at will; contractors would arrogantly violate obligations; and chaos would prevail. In the United States, business and society often share the same values: rugged individualism in a free-enterprise system, pragmatism over abstraction, freedom, and independence. When business practices violate these American values, society and the public are threatened.

Finally, the belief that businesses operate in totally "free markets" is debatable. Although the value or desirability of the concept of a "free market" is not in question, practices of certain firms in free markets are. At issue are the unjust methods of accumulation and noncompetitive uses of wealth and power in the formation of monopolies and oligopolies (i.e., small numbers of firms dominating the rules and transactions of certain markets). The dominance of AT&T before its breakup is an example of how one powerful conglomerate could control the market. Microsoft and Wal-Mart are examples. The U.S. market environment can be characterized best as a "mixed economy" based on free-market mechanisms, but not limited to or explained only by them. Mixed economies rely on some governmental policies and laws for control of deficiencies and inequalities. For example, protective laws are still required, such as those governing minimum wage, antitrust situations, layoffs from plant closings, and instances of labor exploitation. In such mixed economies in which injustices thrive, ethics is a lively topic.

Myth 3: Ethics in Business Is Relative

In this myth, no right or wrong way of believing or acting exists. Right and wrong are in the eyes of the beholder.

The claim that ethics is not based solely on absolutes has some truth to it. However, to argue that all ethics is relative contradicts everyday experience. For example, the view that because a person or society believes something to be right makes it right is problematic when examined. Many societies believed in and practiced slavery; however, in contemporary individuals' experiences, slavery is morally wrong. When individuals and firms do business in societies that promote slavery, does that mean that the individuals and firms must also condone and practice slavery? The simple logic of relativism, which is discussed in Chapter 2, gets complicated when seen in daily experience. The question that can be asked regarding this myth is: Relative to whom or what? And why? The logic of this ethic, which answers that question with "Relative to me, myself, and my interests" as a maxim, does not promote community. Also, if ethical relativism were carried to its logical extreme, no one could disagree with anyone about moral issues because each person's values would be true for him or her. Ultimately, this logic would state that no right or wrong exists apart from an individual's or society's principles. How could interactions be completed if ethical relativism was carried to its limit? Moreover, the U.S. government, in its vigorous pursuit of Microsoft, certainly has not practiced a relativist style of ethics.

Myth 4: Good Business Means Good Ethics

This myth can translate to "Executives and firms that maintain a good corporate image, practice fair and equitable dealings with customers and employees, and earn profits by legitimate, legal means are de facto ethical." Such firms, therefore, would not have to be concerned explicitly with ethics in the workplace. Just do a hard, fair day's work, and that has its own moral goodness and rewards.[49]

The faulty reasoning underlying this logic obscures the fact that ethics does not always provide solutions to technical business problems. Moreover, as Buchholz argued, no correlation exists between "goodness" and material success.[50]

It also argued that "excellent" companies and corporate cultures have created concern for people in the workplace that exceeds the profit motive. In these cases, excellence seems to be related more to customer service, to maintenance of meaningful public and employee relationships, and to corporate integrity than to profit motive.[51]

The point is that ethics is not something added to business operations; ethics is a necessary part of operations. A more accurate, logical statement from business experience would suggest that "good ethics means good business." This is more in line with observations from successful companies that are ethical first and also profitable.

Finally, the following questions need to be asked: What happens, then, if what should be ethically done is not the best thing for business? What happens when good ethics is not good business? The ethical thing to do may not always be in the best interests of the firm. We should promote business ethics, not because good ethics is good business, but because we are morally required to

adopt the moral point of view in all our dealings with other people—and business is no exception. In business, as in all other human endeavors, we must be prepared to pay the costs of ethical behavior. The costs may sometimes seem high, but that is the risk we take in valuing and preserving our integrity.[52]

Myth 5: Information and Computing Are Amoral

This myth holds that information and computing are neither moral nor immoral—they are amoral. They are in a "gray zone," a questionable area regarding ethics. Information and computing have positive dimensions, such as empowerment and enlightenment through the ubiquitous exposure to information, increased efficiency, and quick access to online global communities. It is also true that information and computing have a dark side: information about individuals can be used as "a form of control, power, and manipulation."[53]

The point here is to beware the dark side: the misuse of information, social media, and computing. Ethical implications are present but veiled. Truth, accuracy, and privacy must be protected and guarded: "Falsehood, inaccuracy, lying, deception, disinformation, misleading information are all vices and enemies of the Information Age, for they undermine it. Fraud, misrepresentation, and falsehood are inimical to all of them."[54]

Logical problems occur in all five of the above myths. In many instances, the myths hold simplistic and even unrealistic notions about ethics in business dealings. In the following sections, the discussion about the nature of business ethics continues by exploring two questions:

- Why use ethical reasoning in business?
- What is the nature of ethical reasoning?

1.5 Why Use Ethical Reasoning in Business?

Ethical reasoning is required in business for at least three reasons. First, many times laws do not cover all aspects or "gray areas" of a problem.[55] How could tobacco companies have been protected by the law for decades until the settlement in 1997, when the industry agreed to pay $368.5 billion for the first 25 years and then $15 billion a year indefinitely to compensate states for the costs of health care for tobacco-related illnesses? What gray areas in federal and state laws (or the enforcement of those laws) prevailed for decades? What sources of power or help can people turn to in these situations for truthful information, protection, and compensation when laws are not enough?

Second, free-market and regulated-market mechanisms do not effectively inform owners and managers how to respond to complex issues that have far-reaching ethical consequences. Enron's former CEO Jeffrey Skilling believed that his new business model of Enron as an energy trading company was the next big breakthrough in a free-market economy. The idea was innovative and creative; the executive's implementation of the idea was illegal. Perhaps

Skilling should have followed Enron's ethics code; it was one of the best available.

A third argument holds that ethical reasoning is necessary because complex moral problems require "an intuitive or learned understanding and concern for fairness, justice, [and] due process to people, groups, and communities."[56] Company policies are limited in scope in covering human, environmental, and social costs of doing business. Judges have to use intuition and a kind of learn-as-you-go approach in many of their cases. In Microsoft's previous alleged monopoly case, for example, there were no clear precedents in the software industry—or with a company of Microsoft's size and global scope—to offer clear legal direction. Ethics plays a role in business because laws are many times insufficient to guide action.

1.6 Can Business Ethics Be Taught and Trained?

Because laws and legal enforcement are not always sufficient to help guide or solve complex human problems relating to business situations, some questions arise: Can ethics help? If so, how? And can business ethics be taught? This ongoing debate has no final answer, and studies continue to address the issue. One study, for example, that surveyed 125 graduate and undergraduate students in a business ethics course at the beginning of a semester showed that students did not reorder their priorities on the importance of 10 social issues at the end of the semester, but they did change the degree of importance they placed on the majority of the issues surveyed.[57] What, if any, value can be gained from teaching ethical principles and training people to use them in business?

This discussion begins with what business ethics courses cannot or should not, in my judgment, do. Ethics courses should not advocate a set of rules from a single perspective or offer only one best solution to a specific ethical problem. Given the complex circumstances of many situations, more desirable and less desirable courses of action may exist. Decisions depend on facts, inferences, and rigorous, ethical reasoning. Neither should ethics courses or training sessions promise superior or absolute ways of thinking and behaving in situations. Informed and conscientious ethical analysis is not the only way to reason through moral problems.

Ethics courses and training can do the following:

- Provide people with rationales, ideas, and vocabulary to help them participate effectively in ethical decision-making processes
- Help people "make sense" of their environments by abstracting and selecting ethical priorities
- Provide intellectual insights to argue with advocates of economic fundamentalism and those who violate ethical standards
- Enable employees to act as alarm systems for company practices that do not meet society's ethical standards
- Enhance conscientiousness and sensitivity to moral issues, and commitment to finding moral solutions

- Enhance moral reflectiveness and strengthen moral courage
- Increase people's ability to become morally autonomous, ethical dissenters, and the conscience of a group
- Improve the moral climate of firms by providing ethical concepts and tools for creating ethical codes and social audits[58]

Other scholars argue that ethical training can add value to the moral environment of a firm and to relationships in the workplace in the following ways:

- Finding a match between an employee's and employer's values
- Managing the push-back point, where an employee's values are tested by peers, employees, and supervisors
- Handling an unethical directive from a boss
- Coping with a performance system that encourages cutting ethical corners[59]

Teaching business ethics and training people to use them does not promise to provide answers to complex moral dilemmas. However, thoughtful and resourceful business ethics educators can facilitate the development of awareness of what is ethical, help individuals and groups realize that their ethical tolerance and decision-making styles decrease unethical blind spots, and enhance discussion of moral problems openly in the workplace.

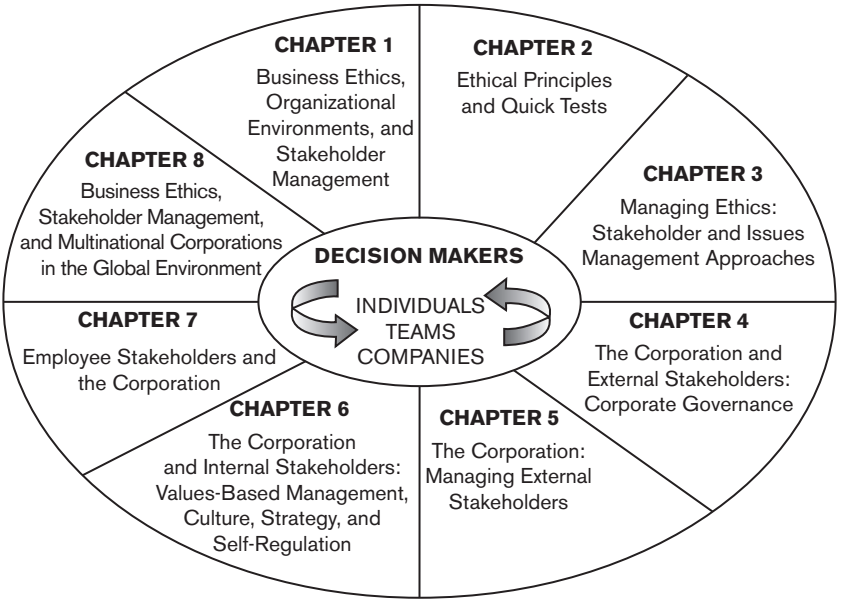
1.7 Plan of the Book

This book focuses on applying a stakeholder management approach—based on stakeholder theory—that is integrated with issues management approaches, along with your own critical reasoning to situations that involve groups and individuals who often have competing interpretations of a problem or opportunity. We are all stakeholders in many situations, whether with our friends, network of colleagues, or in organizational and work settings. Because stakeholders are people, they generally act on beliefs, values, and financially motivated strategies. For this reason, ethics- and values-based thinking is an important part of a stakeholder and issues management approach. It is important to understand why stakeholders act and how they make decisions. The stakeholder and issues management approach aims at having all parties reach win–win outcomes through communication and collaborative efforts. Unfortunately, this does not always happen. If we do not have a systematic approach to understanding what happens in complex stakeholder relationships, we cannot learn from past mistakes or plan for more collaborative, socially responsible future outcomes. A schematic of the book's organization is presented in Figure 1.6.

Chapter 2 provides a foundation of ethical principles, quick tests, and scenarios for evaluating motivations for certain decisions and actions. A stakeholder management approach involves knowing and managing stakeholders' ethics, including your own. Chapter 3 provides a systematic approach for structuring and evaluating stakeholder issues, strategies, and options at the out-

Figure 1.6

Plan of the Book



set. Step-by-step methods for collaborating and for forming and evaluating strategies are identified. Chapter 4 then examines an organization's corporate governance and compliance before Chapter 5 looks at how organizations manage external and business issues stakeholders. Chapter 6 looks at internal stakeholders, strategy, culture, and self-regulation in corporations and discusses rights and obligations of employees and employers as stakeholders. Chapter 7 analyzes current trends affecting employees in corporations and Chapter 8, the final chapter, examines globalization and views nations as stakeholders to examine how multinational corporations operate in host countries and different systems of capitalism.

Chapter Summary

Businesses and governments operate in numerous environments, including technological, legal, social, economic, and political dimensions. Understanding the effects of these environmental forces on industries and organizations is a first step in identifying stakeholders and the issues that different groups must manage in order to survive and compete. This book explores and illustrates how stakeholders can manage issues and trends in their changing environments in socially responsible, principled ways. Thinking and acting ethically is not a mechanical process; it is also very personal. It is important as a professional in an organization, to integrate personal with professional experiences and values.

Business ethics deals with what is "right" and "wrong" in organizational decisions, behavior, and policies. Business ethics provides principles and guidelines that assist people in making informed choices that balance economic interests and social responsibilities. Being able to think of other stakeholders' interests can better inform the moral dimension of your own decisions. This is one aim of using a stakeholder management approach.

Seeing the "big picture" of how ethical issues begin and transform requires imagination and some "maps." Because business ethics apply to several levels, this chapter has presented these levels to illustrate the complexity of ethical decision making in business transactions. When you can "connect the dots" among these dimensions, more options for solving problems morally are opened.

The stakeholder management approach also provides a means for mapping complicated relationships between the focal and other stakeholders, a means of identifying the strategies of each stakeholder, and a means for assessing the moral responsibility of all the constituencies.

Five common myths about business ethics have been discussed. Each myth has been illustrated and refuted. You are invited to identify and question your own myths about business ethics. Ethical reasoning in business is explained with steps to guide decision making. Here are three reasons why ethical reasoning is necessary in business: (1) laws are often insufficient and do not cover all aspects or "gray areas" of a problem; (2) free-market and regulated-market mechanisms do not effectively inform owners and managers on how to respond to complex crises that have far-reaching ethical consequences; and (3) complex moral problems require an understanding and concern for fairness, justice, and due process. Ethical reasoning helps individuals sort through conflicting opinions and information in order to solve moral dilemmas.

Ethical education and training can be useful for developing a broad awareness of the motivations, values, and consequences of our decisions. Business ethics does not, however, provide superior or universally correct solutions to morally complex dilemmas. Principles and guidelines are provided that can enhance—with case analysis, role playing, and group discussion—a person's insight and self-confidence in resolving moral dilemmas that often have two right (or wrong) solutions.

Questions

1. Refer to Figure 1.1 to identify three specific environmental influences that the organization for which you work (or the institution in which you study) must address to survive and be competitive. Explain how these influences, pressures, and opportunities affect you, and ask yourself how ethically do you accomplish your work and goals.
2. What are the three major ethical issues you face now in your work or student life? What is "ethical" about these issues?
3. Identify some benefits of using a stakeholder approach in ethical decision making. How would using a stakeholder management approach help you plan and/or solve an ethical issue in your working life? Explain.

4. What is a myth? Which, if any, of the five business myths discussed in this chapter do you not accept as a myth (i.e., that you believe is true)? Explain.
5. Identify one myth you had/have about business ethics. Where did it originate? Why is it a "myth"? What led you to abandon this myth, or do you still believe in it? Explain.
6. Identify three reasons presented in this chapter for using ethical reasoning in business situations. Which of these reasons do you find the most valid? The least valid? Explain.
7. Is the law sufficient to help managers and employees solve ethical dilemmas? Explain and offer an example from your own experiences or from a contemporary event.
8. What are some important distinctive characteristics of ethical problems? What distinguishes an ethical from a legal problem?
9. What (if any) specific attitudes, values, beliefs, or behaviors of yours do you think could be changed from an ethics course? Explain.
10. Identify and describe a specific belief or behavior of yours that you feel could be changed through taking a course in ethics.

Exercises

1. Invent and state your own definition of "business ethics." Do you believe that ethics is an important factor in business transactions today? If you were the CEO of a corporation, how would you communicate your perspective on the importance of ethics to your employees, customers, and other stakeholder groups?
2. Conduct your own small survey of two people regarding their opinions on the importance of unethical practices in businesses today. Do your interviewees give more importance to economic performance or socially irresponsible behavior? Or do they think other factors are more important? Summarize your results.
3. You are giving a speech at an important community business association meeting. You are asked to give a presentation called "An Introduction to Business Ethics" for the members. Give an outline of your speech.
4. Explain how a major trend in the environment has affected your profession, job, or skills—as a professional or student. Be specific. Are any ethical consequences involved, and has this trend affected you?
5. Review Kohlberg's levels and stages of moral development. After careful consideration, briefly explain which stage, predominantly or characteristically, defines your ethical level of development. Explain. Has this stage influenced a recent decision you have made or action you have taken? Explain.
6. You are applying to a prestigious organization for an important, highly visible position. The application requires you to describe an ethical dilemma in your history and how you handled it. Describe the dilemma and your ethical position.

Real-Time Ethical Dilemma

You are a staff associate at a major public accounting firm and graduated from college two years ago. You are working on an audit for a small, nonprofit religious publishing firm. After performing tests on the royalty payables system, you discover that for the past five years, the royalty payable system has miscalculated the royalties it owes to authors of their publications. The firm owes almost $100,000 in past due royalties. All of the contracts with each author are negotiated differently. However, each author's royalty percentage will increase at different milestones in books sold (i.e., 2% up to 10,000 and 3% thereafter). The software package did not calculate the increases, and none of the authors ever received their increase in royalty payments. At first you can't believe that none of the authors ever realized they were owed their money. You double check your calculations and then present your findings to the senior auditor on the job. Much to your surprise, his suggestion is to pass over this finding. He suggests that you sample a few additional royalty contracts and document that you expanded your testing and found nothing wrong. The firm's audit approach is well documented in this area and is firmly based on statistical sampling. Because you had found multiple errors in the small number of royalty contracts tested, the firm's approach suggested testing 100% of the contracts. This would mean (1) going over the budgeted time/expense estimated to the client; (2) possibly providing a negative audit finding; and (3) confirming that the person who audited the section in the years past may not have performed procedures correctly.

Based on the prior year's work papers, the senior auditor on the job performed the testing phase in all of these years just before his promotion. For some reason, you get the impression that the senior auditor is frustrated with you. The relationship seems strained. He is very intense, constantly checking the staff's progress in the hope of coming in even a half-hour under budget for a designated test/audit area. There's a lot of pressure, and you don't know what to do. This person is responsible for writing your review for your personnel file and bonus or promotion review. He is a very popular employee who is "on the fast track" to partnership.

You don't know whether to tell the truth and risk a poor performance review and jeopardize your future with this company, or to tell the truth, hopefully be exonerated, and be able to live with yourself by "doing the right thing" and facing consequences with a clean conscience.

Questions

1. What would you do as the staff associate in this situation? Why? What are the risks of telling the truth for you? What are the benefits? Explain.
2. What is the "right" thing to do in this situation? What is the "smart" thing to do for your job and career? What is the difference, if there is one, between the "right" and "smart" thing to do in this situation? Explain.
3. Explain what you would say to the senior auditor, your boss, in this situation if you decided to tell the truth as you know it.

Cases

Case 1

Bernard L. Madoff Investment Securities LLC: Wall Street Trading Firm

Bernard L. Madoff Investment Securities LLC was founded in the 1960s as a small investment firm on Wall Street. With $5,000 in savings from summer jobs and at the age of 22, Madoff launched the firm that in the 1980s would later rank with some of the most prestigious and powerful firms on Wall Street. Madoff began as a single stock trader before starting a family-operated business that included his brother, nephew, niece, and his two sons. Each held a position that was quite valuable within the company.

Madoff had also created "an investment-advisory business that managed money for high-net-worth individuals, hedge funds and other institutions." He made profitable and consistent returns by repaying early investors from the money received from new investors. Instead of running an actual hedge fund, Madoff held this investment operation inside his firm on the seventeenth floor of the building where only two dozen staff members were permitted to enter the secured area. No employee dared question the security and confidentiality of the "hedge fund" floor due to the prestige and power that Madoff held. The $65 billion investment fund was later discovered to be fraudulent, involving one of the largest Ponzi schemes in history and shattering the lives of thousands of individuals, institutions, organizations, and stakeholders worldwide.

The Man with All the Power

Bernard Madoff's charisma and amiable personality were important traits that helped him gain power in the financial community and become one of the largest key players on Wall Street. He became a notable authoritative figure by securing important roles on boards and commissions, helping him bypass securities regulations. One of the roles included serving as the chairman of the board and directors of the NASDAQ stock exchange during the early 1990s. Madoff was knowledgeable and smart enough to understand that the more involved he became with regulators, the more "you could shape regulations." He used his reputation as a respected trader and perceived "honest" businessman to take advantage of investors and manipulate them fraudulently. Investors were hoodwinked into believing that it was a privilege to take part in Madoff's elite investments, since Madoff never accepted many clients and used exclusively selective recruiting in order to keep this part of his business a secret.

Madoff was even able to keep his employees quiet, telling them not to speak to the media regarding any of the business activities. While several understood something was not right, they ignored suspicions due to Madoff's perceived clean record and aura: "He appeared to believe in family, loyalty, and honesty. . . . Never in your wildest imagination would you think he was a fraudster."

Dr. Meloy, author of the textbook *The Psychopathic Mind,* states that "typically people with psychopathic personalities don't fear getting caught. . . . They tend to be very narcissistic with a strong sense of entitlement." This led many analysts of criminal behavior to observe similar traits between Madoff and serial killers like Ted Bundy. Analysts discovered several factors motivating Madoff toward a Ponzi scheme: "A desire to accumulate vast wealth, a need to dominate others, and a need to prove that he was smarter than everyone else." Whatever the motivating factors were, Madoff's behavior was still criminal and affected a large pool of stakeholders.

Early Suspicions Arise

Despite the unrealistic returns and questionable nature of Madoff's business operations, investors continued to invest money. In 2000, a whistle-blower from a competing firm—Harry Markopolos, CFE, CFA—discovered Madoff's Ponzi scheme. Markopolos and his small team developed and presented an eight-page document that provided evidence and red flags of the fraud to the Securities and Exchange Commission (SEC)'s Boston Regional Office in May 2000. Despite the SEC's lack of response, Markopolos resubmitted the documents again in 2001, 2005, 2007 and 2008. His findings were not taken seriously: "My team and I tried our best to get the Securities and Exchange Commission (SEC) to investigate and shut down the Madoff Ponzi scheme with repeated and credible warnings." Because Madoff was well respected and powerful on Wall Street, few suspected his fraudulent actions. The status and wealth that Madoff had created gave him the means to manipulate the SEC and regulators alike.

Negligence on All Sides

The negligence and gaps in governmental regulation make it very difficult to point to only one guilty party in the Madoff scandal. The SEC played a crucial role by allowing Madoff's operations to carry out for as long as they did. For over 10 years, the SEC received numerous warnings that Madoff's steady returns were anything but ordinary and nearly impossible. The SEC and the Financial Industry Regulatory Authority, "a non-government agency that oversees all securities firms," were known to have investigated Madoff's firm over eight times but brought no charges of criminal activity. Despite the red flags and mathematical proof that Markopolos presented, SEC staff allowed Madoff's operations to continue unchallenged. Spencer Bachus, a politician and a Republican member of the U.S. House of Representatives, stated that "What we may have in the Madoff case is not necessarily a lack of enforcement and oversight tools, but a failure to use them." Unfortunately, there could be another side to the story. David Kotz, currently the SEC's inspector general, planned an ongoing internal investigation to understand the reasoning behind the negligence and to determine if any conflict of interest between SEC staff and the Madoff family could have been part of the problem. Arthur Levitt Jr., who was part of the SEC and a chairman from 1993 to 2001, had close connections with Madoff himself. He would rely on

Madoff's advice about the functioning of the market, although Levitt denies all accusations. In September 2009, it was officially stated that no evidence was found relating to any conflict of interest: "The OIG [Office of Inspector General] investigation did not find evidence that any SEC personnel who worked on an SEC examination or investigation of Bernard L. Madoff Investment Securities LLC had any financial or other inappropriate connection with Bernard Madoff or the Madoff family that influenced the conduct of their examination or investigatory work."

Unfortunately, the SEC is not the only party to blame. JPMorgan Chase has also been criticized for its actions regarding the Madoff scandal. Instead of investing client's money in securities, as Madoff had promised to do, he deposited the funds in a Chase bank account. In 2008, federal court documents show that "the account had mushroomed to $5.5 billion. . . . This translates to $483 million in after-tax profits for the bank holding the Madoff funds." As one of Chase's largest customers, Madoff's account should have been monitored closely. Internal bank compliance systems should have detected such red flags. Unfortunately, Madoff was savvy enough to move millions of dollars between his U.S. and London operations, making it seem like he was actively investing clients' money. The massive account balances of investors should not have been difficult to overlook. Don Jackson, director of the SecureWorks Counter Threat Unit Intelligence Services, noted that "The only way to stop this kind of fraud is for the bank to know its clients better and to report things that might be suspicious. It really comes down to human control." This was an area of weakness for JPMorgan Chase at the time.

Where Were the Auditors?

For Madoff to successfully perpetrate such a large scam spanning more than a decade, he needed the help of auditors to certify the financial statements of Bernard L. Madoff Investment Securities. The company's auditing services were provided by a three-person accounting firm, Friehling & Horowitz, formerly run by David Friehling. For over 15 years, Friehling confirmed to the American Institute of Certified Public Accountants (AICPA) that his firm did not conduct any type of audit work. Because of this confirmation, Friehling did not have to "enroll in the AICPA's peer review program, in which experienced auditors assess each firm's audit quality every year . . . to maintain their licenses to practice." Friehling & Horowitz had in fact been auditing the books of Madoff for over 17 years, providing a clean bill of health each year from 1991 through 2008. Authorities state that if Friehling provided integrity in his findings, the scandal would not have continued for as long as it did: "Mr. Friehling's deception helped foster the illusion that Mr. Madoff legitimately invested his client's money," stated U.S. Attorney Lev Dassin. In addition to receiving total fees of $186,000 annually from the auditing services provided to Madoff, Friehling also had accounts in Madoff's firm totaling more than $14 million and had withdrawn over $5.5 million since the year 2000. Friehling deceived investors and regulators by providing unauthorized audit work and verifying fraudulent financial statements. Given the size of the

accounting firm, a red flag should have been raised. Madoff's operations were too large in size and complexity for the resources of a three-person accounting firm.

Revealing the Fraud

As the U.S. economy entered the 2008 recession period, investors began to panic and withdraw their money from Madoff's accounts, totaling more than $7 billion. Madoff was unable to cover the redemptions and struggled "to obtain the liquidity necessary to meet those obligations." He confessed to his sons that the business he was running was a scam. On December 11, 2008, Bernard Madoff was arrested by federal agents—one day after his sons reported his confession to the authorities.

Global Crisis

The Ponzi scheme that Madoff ran for more than a decade affected the lives of thousands of individuals, institutions, organizations, and stakeholders worldwide. A 162-page list was submitted to the U.S. Bankruptcy Court in Manhattan detailing the affected parties. The lengthy list consisted of some of the wealthiest investors and well-known names around the region: "They reportedly include Philadelphia Eagles owner Norman Braman, New York Mets owner Fred Wilpon and J. Ezra Merkin, the chairman of GMAC Financial Services." Talk show host Larry King and actor John Malkovich were on the list, among others. Many investment-management firms, such as Tremont Capital Management and Fairfield Greenwich Advisors, had invested large amounts in Madoff's funds and were hit the hardest financially. Major global banks, "including Royal Bank of Scotland, France's largest bank, BNP Paribas, Britain's HSBC Holdings PLC and Spain's Santander" were also known to have lost millions. Charitable foundations, such as the Lautenberg foundation; and financial institutions, including Bank of America Corp., Citigroup, and JPMorgan Chase were all stakeholders in the Madoff scandal. Ordinary individuals also invested much of their life savings into what they believed was a "once in a lifetime opportunity." William Woessner, a retiree from the State Department's Foreign Service, agreed that the investors "were made to feel that it was a big favor to be let in if you didn't have a lot of money. It was an exclusive club to belong to." It has been reported that individual losses were between $40,000 to over $1 million in total. There were 3,500 investors from New York and more than 1,700 from Florida.

The repercussions of Madoff's Ponzi scheme have been emotional as well as financial. A French aristocrat and professional investor living within the suburbs of New York, Rene-Thierry Magon de la Villehuchet, had invested almost $1.4 billion in Madoff's accounts. He had invested both his and his client's money, only to lose everything. Villehuchet felt personally responsible for the loss of his clients' money: "He had a true concept of capitalism. . . . He felt responsible and he felt guilty," said his brother Bertrand de la Villehuchet. Villehuchet's depression grew to such a point that he committed suicide on December 22, 2008.

Consequences and Aftermath

On June 29, 2009, Judge Denny Chin found Madoff guilty on eleven criminal counts and sentenced him to 150 years in prison, the maximum possible sentence allowed at the time. Chin's severe sentence was influenced by the statements given by Madoff's victims and the 113 letters received and filed with the federal court: "A substantial sentence may in some small measure help the victims in their healing process," stated Judge Chin. Madoff was also forced to pay a $170-billion legal judgment passed by the government, stating that this amount of money "was handled by his firm since its founding in the 1960s." David Friehling, the auditor for Madoff's books, was also arrested on fraud charges. He was initially "released on a $2.5-million bond and had to surrender his passport." Friehling lost his CPA license in 2010, and his sentencing has since been postponed four times. He faces a sentence of more than 100 years in prison.

Lawyer Irving H. Picard is a bankruptcy trustee in the Madoff scandal. As a court-appointed trustee, Picard has filed numerous lawsuits and has collected $1.2 billion in recovered funds from "banks, personal property, and funds around the world." It is estimated that from this $1.2 billion, Picard has earned approximately $15 million. More than $116 million has been given to 237 Madoff victims, each receiving up to $500,000. In order to help the victims of the Madoff scandal, Picard started a program called "Hardship Case." He has also filed a $199 million lawsuit against the Madoff family, including Madoff's brother, his two sons, and niece, all of whom worked alongside Madoff. An additional lawsuit was filed against Madoff's wife for $44.8 million, stating that she had transferred large amounts of money from the firm "over a six-year period." As of now, none of the family members—Madoff's two sons, brother, niece, and wife—have been found guilty on any of the charges. Madoff's oldest son, Mark, 46, committed suicide in December 2010. Madoff's victims took swift action against the negligence of SEC and JPMorgan Chase. U.S. District Court Judge Colleen McMahon threw out most of the $19.9 million charges against JPMorgan in November 2011, however. The New York Mets owners paid a settlement of $162 million in March of 2012 to avoid going to trial to answer the allegations made by Irving Picard.

Hidden Secrets?

Despite the accusations of negligence that JPMorgan Chase received from the public, it was one of the biggest-profiting financial firms in the Madoff scandal. As stated earlier in the case, JPMorgan made a profit of $483 million. During 2006, "the bank had started offering investors a way to leverage their bets on the future performance of two hedge funds that invested with Mr. Madoff" and decided to place $250 million of their own money inside these funds. A few months before Madoff's arrest in 2008, JPMorgan withdrew its $250 million, stating that it had become "concerned about the lack of transparency and its due diligence raised doubts about Madoff's operations." It is surprising that the bank was suspicious and apprehensive toward investments with Madoff, but at the same time raised no concerns about the large amount of money being

deposited in Madoff's accounts within the bank. JPMorgan also failed to alert investors to move their money, stating that "The issues did not meet the threshold necessary to permit the bank to restructure the notes. . . . We did not have the right to disclose our concerns." Regardless of the public statements made by JPMorgan in support of its actions, many lawyers and investors believe that the bank had knowledge of Madoff's scam but wanted to secure high returns for as long as possible.

Ethical Flaws

In a 2011 *New York Magazine* interview, Madoff stated that he never thought the collapse of his Ponzi scheme would cause the sort of destruction that has befallen his family. He asserted that unidentified banks and hedge funds were somehow "complicit" in his elaborate fraud, an about-face from earlier claims that he was the only person involved. "They had to know," Mr. Madoff said. "But the attitude was sort of, 'If you're doing something wrong, we don't want to know.' " To date, none of the major banks or hedge funds that did business with Mr. Madoff have been accused by federal prosecutors of knowingly investing in his Ponzi scheme. However, in civil lawsuits Picard has asserted that executives at some banks expressed suspicions for years, yet continued to do business with Madoff and steer their clients' money into his hands.

In some ways, Madoff has not tried to evade blame. He has made a full confession, saying that nothing justifies what he did. And yet, for Madoff, that doesn't settle the matter. He feels misunderstood. He can't bear the thought that people think he's evil. "I'm not the kind of person I'm being portrayed as," he told *New York Magazine*.

A main issue in this controversy is the continuous fraudulent operations that Madoff was able to maintain for a decade that created a $65 billion Ponzi scheme and shattered the lives of thousands around the world. For most of the world, Bernie Madoff is a monster: he betrayed thousands of investors, and bankrupted charities and hedge funds. On paper, his Ponzi scheme lost nearly $65 billion; the effects spread across five continents. And he brought down his own family with him, a more intimate kind of betrayal.

Bernard Madoff was the central stakeholder who manipulated and involved his brother, two sons, and niece, all of whom worked inside the Bernard L. Madoff Investment Securities LLC. Other key stakeholders included Madoff's employees, who had invested their money into an operation they believed was legal and ethical. The financial community were also major players, including financial institutions, investment management firms, charitable organizations, and global banks. The government, specifically the SEC, and the justice department, were also heavily involved. The lawyer Irving Picard was a key player, as was the whistleblower Harry Markopolos and his team who revealed the nature of the scam early on, even though the SEC and other government regulators did not move on the evidence.

As of October 2013, Federal authorities are working toward mounting a criminal investigation into JPMorgan Chase, believing that the bank may have

intentionally neglected Madoff's Ponzi scheme. Having recently agreed to a $13 billion settlement with the U.S. government to settle charges that the bank overstated the quality of mortgages it was selling to investors in the run-up to the financial crisis, the threat of criminal charges over the Madoff case represents another major threat to the reputation of the nation's largest bank. The resolution of this scheme is not over.

Questions for Discussion

1. What did Madoff do that was illegal and unethical?
2. Identify some of the main reasons that Madoff was able to start and sustain such an enormous Ponzi scheme for as long as he did?
3. Who were/are the major stakeholders involved and affected by Madoff's scheme and scandal?
4. Did Madoff have accomplices in starting and sustaining his scheme or was he able to do it alone? Explain.
5. How was he caught?
6. What lessons can be learned from Madoff's scandal?

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Case 2

Cyberbullying: Who's to Blame and What Can Be Done?

What Is Cyberbullying?

Cyberbullying is a unique form of bullying that continues in spite of the dire consequences that can and do occur. Cyberbullying has gained significant media attention and countless incidents of bullying continue to occur. Although many cases are reported in the news, probably as many if not more go unreported. Because of the news attention, the phenomenon generated an antibullying movement in 2010. Bullying has been defined as something that one repeatedly does or says to gain power over another person. Unlike traditional bullying, cyberbullying eliminates the need for physical contact with others in order to make them feel inferior. Cyberbullying is "when a child, preteen or teen is tormented, threatened, harassed, humiliated, embarrassed or otherwise targeted by another child, preteen or teen using the Internet, interactive and digital technologies or mobile phones."[1] Technology as an avenue for intimidation is a hot-button issue for school systems and parents alike. This is uncharted territory, and legislation does not always provide guidance and structure.

The reality is that bullying makes a significantly negative impact on the lives of today's youth. Cyberbullying directly impacts self-esteem and can, and has, led to suicide among its adolescent victims. Schools, parents, and peers must identify and intervene in cases of cyber bullying. Increased awareness and education about cyber bullying and its consequences can help create a safer online community. Individuals should be held morally responsible for the consequences of their actions online.

Why Cyberbullying?

A young adult's behavior is primarily motivated by a desire to meet his or her basic need for recognition, attention, and approval. In a survey conducted in 1999, students in over 100 schools were asked the following question: "Is it easier for you to get noticed or get attention in this school by doing something positive or something negative?" Almost 100% replied "negative."[2] Adolescents turn to cyberbullying to fuel their need for attention and recognition from their peers. It began primarily in chat rooms and instant messaging conversations, but has expanded to include social networking web sites (Facebook and MySpace) and video-sharing web sites (YouTube). Text messaging and anonymous web postings are common methods of cyberbullying. Very recently, cyberbullying has established a presence in portable gaming devices through "virtual worlds" and interactive sites.

Cyberbullying is more attractive than traditional bullying for a variety of reasons. First, technology provides the perpetrator with the option of anonymity. Victims often do not know who is targeting them because the bully is able to hide his or her identity through anonymous web posts or fictitious e-mails. Secondly, bullies are able to expand the scope of their impact because a larger

network of individuals may be involved in the cyber-attack. With just a few mouse clicks, an entire community may be a participant in the incident, creating the perception that "everyone" knows about it. Many argue that it is psychologically easier to be a cyberbully than a traditional bully. A cyberbully does not have to physically confront the victim and witness the immediate result of a message. Some cyberbullies might not even recognize the severity of their actions, which take place from a different location. Lastly, the response to cyberbullying has been slow, suggesting to perpetrators that there are little or no consequences for malicious online actions.

Why Is Cyberbullying a Major Issue?

Today's youth are "wired" and connected to technology 24/7. Statistics suggest that "two-thirds of [American] youth go online every day for school work, to keep in touch with their friends, to play games, to learn about celebrities, to share their digital creations, or for many other reasons."[3] Given the accessibility of technology, it should be no surprise that individuals are using the Internet, cell phones, and other electronic instruments to bully each other. A 2010 study revealed that "30% of middle school students were victims of at least one of nine forms of cyber bullying two or more times in the past 30 days" and "22% of middle school students admitted to engaging in at least one of five forms of cyber bullying two or more times in the past 30 days."[4] Females are more likely to choose cyberbullying over traditional bullying. The rationale is that females prefer the nonconfrontational nature of technology.

With such a large percentage of today's youth affected by cyberbullying, something has to be done. Cyberbullying is damaging to the self-esteem of the victims. Typically beginning around middle school, self-perception begins to dictate a child's sense of self-worth. Teenagers often feel that they are defined by "their erupting skin and morphing bodies, [and] many seventh-grade students have a hard enough time just walking through the school doors. When dozens of kids vote online, which is not uncommon, about whether a student is fat or stupid or gay, the impact can be devastating."[5] Victims of cyberbullying typically report feeling angry, frustrated, sad, embarrassed, and scared.

An adolescent's self-esteem can dramatically decrease during puberty. In one survey, when kids in kindergarten were asked if they like themselves, 95% or more said "yes." By fourth grade, the percentage of kids who reported liking themselves was down to 60%; by eighth grade the percentage was down to 40%; and by twelfth grade it was down to 5%.

Meet the Victims

Phoebe Prince. On January 14, 2010, Phoebe Prince was found dead in her South Hadley, Massachusetts home. Phoebe was 15 years old and a recent immigrant from Ireland attending South Hadley High School. As a freshman in high school, she had a romantic fling with a senior football player, upsetting the other girls at her school. They tormented her relentlessly, calling her a "slut." They even followed her home one day, throwing things at her from their moving car.

Phoebe took her own life when the intimidation became too much. She was found dead by her 12-year-old sister.

Immediately following the death of Phoebe Prince, the girls who bullied her mocked her death on the Internet. It was confirmed that Phoebe had been a victim of both cyberbullying and daily physical abuse. Many students reported to school officials that Phoebe was the victim of harassment via social networking sites like Facebook and text messages. Two students of South Hadley High School were later suspended as a result. Principal Daniel Smith observed that "the bullying often surrounded arguments about teen dating."[7] Even in her death, a Facebook page created in her memory contained cruel messages posted by bullies.

Megan Meier. Another high-profile case was that of Megan Meier, a 13-year-old girl whose suicide was the result of cyberbullying. In October 2006, Tina and Ron Meier found their daughter's body in a bedroom closet. Megan had hanged herself. A few weeks earlier, Megan established a relationship with a boy using the social networking site MySpace. Megan and the boy, "Josh Evans"—later discovered to be a fake cover name for another (others) to use as Megan's cyberbullies, quickly formed an online relationship. The catch, as noted: Josh Evans was not a real person. Evans claimed to be a 16-year-old boy who lived in a nearby town but was homeschooled. There were several red flags to suggest that Josh Evans did not exist, but to Megan Meier, an already insecure teenager on medication for depression, the boy seemed very real. The so-called Josh even told Megan that he did not have a phone, restricting him to virtual communication.

Megan's online relationship with Josh then took a turn for the worse. Megan received a message from Josh on MySpace saying, "I don't know if I want to be friends with you any longer because I hear you're not nice to your friends." A bully was using Josh's account to send cruel messages. Megan called her mother, describing electronic bulletins posted about her saying things like "Megan Meier is a slut. Megan Meier is fat."[8] Megan had an existing history of depression, and these messages were a crushing blow to her self-esteem. The stress of the situation was too much for Megan, and she took her own life shortly after these messages were posted.

The person orchestrating Josh Evan's fictitious account was actually a neighborhood mother. Lori Drew, aged 47 at the time of Megan's death, was the mother of one of Megan's former friends. Lori Drew knew that Megan had been prescribed antidepressants but still used the fraudulent identity to torment Megan. Drew's reasoning was that Megan had been mean to her daughter and needed to be taught a lesson. This highly unusual case went to trial in November 2008, and Drew was found guilty of three misdemeanors. She did not serve any jail time.

The Beverly Vista School. In May of 2008, Evan S. Cohen confronted the Beverly Vista School in Beverly Hills, California, for disciplining his eighth-grade daughter, J. C. Cohen for cyberbullying. J. C. had videoed friends at a café egging another eighth-grade girl. In the video, J. C. and her friends make mean-spirited comments toward the victim, calling her "ugly," "spoiled," and a "slut." When the

video surfaced online, the Beverly Vista School suspended J. C. for two days, along with her accomplices.

Mr. Cohen, a lawyer in the music industry, sued the school on behalf of his daughter. "What incensed me," he said, "was that these people were going to suspend my daughter for something that happened outside of school."[9] The legal test was whether or not the video had caused the school "substantial" disruption. According to the law, a student can only be suspended when his or her speech interferes "substantially" with the school's educational mission. The judge ruled in favor of Cohen, and the school district was required to pay Cohen's legal expenses amounting to $107,150.80.[10] "The Judge also threw in an aside that summarizes the conundrum that is adolescent development, acceptable civility and school authority. The good intentions of the school notwithstanding, he wrote, it cannot discipline a student for speech, simply because young persons are unpredictable or immature, or because, in general, teenagers are emotionally fragile and may often fight over hurtful comments."[11]

No case involving student online speech has yet been brought before the Supreme Court. Lower courts have ruled both ways, sometimes siding with schools disciplining their students and other times siding with the individual perpetrator.

Legislation for Cyberbullying

In response to these and other cases, the Federal government has taken steps to prevent and to manage cyberbullying, including the drafting of the Megan Meier Cyberbullying Prevention Act (H.R. 1966). This bill proposes that Chapter 41 of Title 18 of the United States Code (related to extortion and threats) be amended to define cyberbullying and related penalties. According to the Act, cyberbullying is not limited to social-networking web sites but also includes e-mail, instant messaging, blogs, web sites, telephones, and text messages. "The bill would amend the federal criminal code to impose criminal penalties on anyone who transmits in interstate or foreign commerce a communication intended to coerce, intimidate, harass, or cause substantial emotional distress to another person, using electronic means to support severe, repeated, and hostile behavior."[12]

The Megan Meier bill was introduced to the House of Representatives on April 2, 2009. It was referred to two subcommittees–the House Judiciary Committee and the House Judiciary Subcommittee on Crime, Terrorism, and Homeland Security. The last action was on September 30, 2009, when subcommittee hearings were held. The bill has not become law. It was a part of a previous session of Congress and must be reintroduced in order to be reconsidered for law.

State governments are also considering laws against cyberbullying. On May 3, 2010, Governor Deval Patrick signed new antibullying legislation that places greater responsibility on schools to intervene in bullying situations. "Bullying, as defined by the bill, encompasses crimes such as stalking and harassment. The anti-bullying legislation specifically holds provisions for anti-bully training, and mandates that all school employees, including teachers, cafeteria staff, janitorial staff, etc., must report and investigate incidents involving bullying. Teachers

must also notify all parents of the students involved in the bullying incident. It also includes an anti-bullying curriculum to be taught in both public and private schools."[13]

Although a step in the right direction, the bill does not assign specific penalties to those who do not intervene in instances of bullying. Following the bill's implementation, bullying continues to be a major issue in Massachusetts schools.

On February 13, 2013, Illinois State Senate representative Ira I. Silverstein introduced the Internet Posting Removal Act–SB 1614. When you read the bill solely through cyberbullying-prevention lenses, it makes sense. But what happens when politicians start using the statute to silence critics? Precise language is a must when it comes to laws; loose lips sink ships and loose language can annihilate freedoms.

The Impact of Facebook and MySpace

The growth of social networking web sites such as Facebook and MySpace in the past decade has contributed to the prevalence of cyberbullying. Both social-networking giants have experience in dealing with cyberbullying. Facebook and MySpace have accessible help centers that provide postings and suggestions on how users can fight back against cyberbullying.

Facebook gives users the responsibility to manage cyberbullying. On Facebook's Help Menu, advisory information is available for teens and parents regarding how to handle cyberbullying. Facebook provides a mechanism for users to report abusive behavior by another user. After the abuse is reported, Facebook investigates the behavior. Facebook also gives users the ability to block specific individuals and restrict privacy settings. There are comprehensive instructions on Facebook's web site to make online safety as user-friendly as possible.

Facebook also encourages users to avoid retaliation, recommending that victims block or report abusers rather than respond via "inbox, wall posting, or Facebook Chat." A section of Facebook's Help Center is dedicated to educating parents about ways to protect their teens from cyberbullying. This page emphasizes the need for communication among parents and teens regarding expectations and the use of common sense. Though Facebook cannot prevent and monitor every issue of online harassment, the company recognizes that cyberbullying is an issue and is doing what it can to empower users.

MySpace, another social-networking leader, recognizes the negative consequences of cyberbullying and has similar content to help its users. MySpace users have the ability to "block" individuals and report instances of harassment. MySpace has a zero tolerance policy for hate speech, harassment, and cyberbullying, and pledges to do its best to respond to reported situations within 48 hours.[14] Parents have the power to delete the contents of their son's or daughter's MySpace page. The web site also provides safety tips for teens and parents, including links to more resources and safety videos.

MySpace has developed a team of specialists to assist parents with inquiries regarding their teens' profiles. The Parent Care Team must be initiated for review by a parent and can perform actions other than simply deleting a teen's profile.

For instance, the Parent Care Team can lock (i.e., fix in place as unchangeable) the age on a teen's profile and answer any questions that a parent may have about their teen's MySpace page. This service is available via e-mail and detailed instructions are available.

Although Facebook and MySpace have taken steps to prevent cyberbullying on their respective web sites, these efforts are not enough. Cyberbullying is still a major issue on social-networking sites and on other forms of media and communication. To push forward to a solution, questions must be raised about who should be held accountable in instances of cyberbullying.

Conclusion

Cyberbullying is a real issue that deserves recognition. We should be educating adolescents about the potentially damaging effects of their actions, responding to incidents, and holding the appropriate people accountable in instances of cyberbullying. All stakeholders in cyberbullying should take this issue very seriously. Cyberbullying can have an incredibly harmful effect on adolescents if nobody intervenes. Teenagers, parents, schools, and the government especially, have a moral responsibility to take action when they come across cyberbullying. From an ethical perspective, we can no longer be bystanders. Take a stand against cyberbullying.

Questions for Discussion

1. Have you or someone you know ever been involved in cyberbullying, as a bully or victim? If so, what are the feelings and effects associated with cyberbullying in the situations with which you are familiar?
2. What are the issues with cyberbullying? Explain.
3. Who are the stakeholders in cyberbullying cases and what are the stakes for them?
4. Who is ethically responsible for the rise and continuance of cyberbullying?
5. Should social-networking sites be censored in an effort to stop cyberbullying? Explain.
6. Is it legal and ethical to censor social-networking sites to stop cyberbullying? Explain.
7. What is Congress doing about this situation?

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2

ETHICAL PRINCIPLES, QUICK TESTS, AND DECISION-MAKING GUIDELINES

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Notes

OPENING CASE

Louise Simms, newly graduated with a Master of Business Administration (MBA) degree, was hired by a firm based in the United States. With minimal training, she was sent to join a company partner to negotiate with a high-ranking Middle Eastern government official. The partner informed Simms that he would introduce her to the government contact and then leave her to "get the job done." Her assignment was to "do whatever it takes to win the contract: it's worth millions to us." The contract would enable Simms's firm to select and manage technology companies that would install a multimillion-dollar computer system for that government. While in the country, Simms was told by the official that Simms's firm had "an excellent chance of getting the contract" if the official's nephew, who owned and operated a computer company in that country, could be assured "a good piece of the action."

On two different occasions, while discussing details, the official attempted unwelcome advances toward Simms. He backed off both times when he observed her subtle negative responses. Simms was told that "the deal" would remain a confidential matter and the official closed by saying, "That's how we do business here; take it or leave it." Simms was frustrated about the terms of the deal and about the advances toward her. She called her superior in Chicago and urged him not to accept these conditions because of the questionable arrangements and also because of the disrespect shown toward her, which she said reflected on the company as well. Simms's supervisor responded, "Take the deal! And don't let your emotions get involved. You're in another culture. Go with the flow. Accept the offer and get the contract groundwork started. Use your best judgment on how to handle the details."

Simms couldn't sleep that night. She now had doubts about her supervisor's and the government administrator's ethics. She felt that she had conflicting priorities. This was her first job and a significant opportunity. At the same time, she had to live with herself.

2.1 Ethical Reasoning and Moral Decision Making

> The ultimate basis for ethics is clear: Much human behavior has consequences for the welfare of others. We are capable of acting toward others in such a way as to increase or decrease the quality of their lives. We are capable of helping or harming. . . . The proper role of ethical reasoning is to highlight acts of two kinds: those that enhance the well-being of others—that warrant our praise—and those who harm or diminish the well-being of others—and thus warrant our criticism. Developing one's ethical reasoning abilities is crucial because there is in human nature a strong tendency toward egotism, prejudice, self-justification, and self-deception.[1]

Ethical reasoning helps determine and differentiate between *right* thinking, decisions, and actions and those that are *wrong*, hurtful and/or harmful—to others and to ourselves. Ethics is based on and motivated by values, beliefs, emotions, and feelings as well as facts. Ethical actions also involve conscientious reasoning of facts based on moral standards and principles. *Business ethics* refers to applying ethical reasoning and principles to commercial activities that are often profit-oriented.

Three Criteria in Ethical Reasoning

The following criteria can be used in ethical reasoning. They help to systematize and structure our arguments:[2]

1. Moral reasoning must be logical. Assumptions and premises, both factual and inferred, used to make judgments should be known and made explicit.

2. Factual evidence cited to support a person's judgment should be accurate, relevant, and complete.
3. Ethical standards used in reasoning should be consistent. When inconsistencies are discovered in a person's ethical standards in a decision, one or more of the standards must be modified.

Returning to this chapter's opening case, if Louise Simms were to use these three criteria, she would articulate the assumptions underlying her decision. If she chose to accept the official's offer, she might reason that she assumed it was not a bribe or that if it were a bribe she would not get caught, and that even if she or her company did get caught, she would be willing to incur any penalty individually, including the loss of her job. Moreover, Louise would want to obtain as many facts as she could about the U.S. laws and the Middle Eastern country's laws on negotiating practices. She would gather information from her employer and check the accuracy of the information against her decision.

She would have to be consistent in her standards. If she chooses to accept the foreign official's conditions, she must be willing to accept additional contingencies consistent with those conditions. She could not suddenly decide that her actions were "unethical" and then back out midway through helping the official's nephew obtain part of the contract. She must think through these contingencies *before* she makes a decision.

Finally, a simple but powerful question can be used throughout your decision-making process: What is my *motivation* and *motive* for choosing a course of action? Examining individual motives and separating these from the known motivations of others provides clarity and perspective. Louise, for example, might ask, "Why did I agree to negotiate with the official on his terms? Was it for money? To keep my job? To impress my boss? For adventure?" She also might ask whether her stated motivation from the outset would carry her commitments through the entire contracting process.

Moral Responsibility Criteria

A major aim of ethical reasoning is to gain a clear focus on problems to facilitate acting in morally responsible ways. Individuals are morally responsible for the harmful effects of their actions when (1) *they knowingly and freely acted or caused the act to happen and knew that the act was morally wrong or hurtful to others* and (2) *they knowingly and freely failed to act or prevent a harmful act, and they knew it would be morally wrong for a person to do this*.[3] Although no universal definition of what constitutes a morally wrong act exists, an act and the consequences of an act can be defined as morally wrong if physical or emotional harm is done to another as a result of the act.

Two conditions that eliminate a person's moral responsibility for causing injury or harm are *ignorance* and *inability*.[4] However, persons who intentionally prevent themselves from knowing that a harmful action will occur are still responsible. Persons who negligently fail to inform themselves about a potentially harmful matter may still be responsible for the resultant action. Of

course, some mitigating circumstances can excuse or lessen a person's moral responsibility in a situation. These include circumstances that show: (1) a low level of or lack of seriousness to cause harm, (2) uncertainty about knowledge of wrongdoing, and (3) the degree to which a harmful injury was caused or averted. As we know from court trials, proving intent for an alleged illegal act is not an easy matter. Legally, a case involving a defendant is generally in jeopardy when there is sufficient physical as well as other evidence demonstrating that a person "knowingly and willingly" showed intent to commit an illegal act. However, the extent to which a person is morally irresponsible can be difficult to determine.

2.2 Ethical Principles and Decision Making

In this section, five fundamental principles used in ethical reasoning that are both classic and timely are discussed to solve dilemmas in everyday life as well as in complex business situations. Observe Figure 2.1 as you read this section. Since we are examining stakeholders in this text, and we all are stakeholders

Figure 2.1

Summary of Five Ethical Decision-Making Principles with Stakeholder Analysis

Belief Systems	Source of Moral Activity	Stakeholder Analysis Issues
Utilitarianism (Calculation of Costs and Benefits)	Moral authority is determined by the consequences of an act: An act is morally right if the net benefits over costs are greatest for the majority. Also, the greatest good for the greatest number must result from this act.	1. Consider collective as well as particular interests.
		2. Formulate alternatives based on the greatest good for all parties involved.
		3. Estimate costs and benefits of alternatives for groups affected.
Universalism (Duty)	Moral authority is determined by the extent to which the intention of an act treats all persons with respect. Includes the requirement that everyone would act this way in the same circumstances.	1. Identify individuals whose needs and welfare are at risk with a given policy or decision.
		2. Identify the use or misuse of manipulation, force, coercion, or deceit that may be harmful to individuals.
		3. Identify duties to individuals affected by the decision.
		4. Determine if the desired action or policy would be acceptable to individuals if the decision were implemented.

Figure 2.1 *–continued*

Belief Systems	Source of Moral Activity	Stakeholder Analysis Issues
Rights (Individual Entitlement)	Moral authority is determined by individual rights guaranteed to all in their pursuit of freedom of speech, choice, happiness, and self-respect.	1. Identify individuals and their rights that may be violated by a particular action.
		2. Determine the legal and moral basis of these individual rights.
		3. Determine the moral justification from utilitarian principles if individuals' rights are violated.
Justice (Fairness and Equity)	Moral authority is determined by the extent opportunities, wealth, and burdens are fairly distributed among all.	1. If a particular action is chosen, how equally will costs and benefits be distributed to stakeholders?
		2. How clear and fair are the procedures for distributing the costs and benefits of the decision?
		3. How can those who are unfairly affected by the action be compensated?
Virtue Ethics (Character-Based Virtues)	Moral authority is based on individual character virtues such as truthfulness, integrity, and honesty. An act, policy, strategy is moral if it reflects these types of virtues.	1. What are the "character virtues" of the individual stakeholder(s), the policy, procedure, or strategy in question?
		2. If a particular action, policy, strategy is chosen, to what extent will these virtues be evident, or missing?
		3. While seeking a mutually desirable outcome in a conflicting situation, how can conflicting character values and characteristics that are embedded and/or reflected in a decision, policy, or strategy be avoided or negotiated?

in different situations, we illustrate how the following principles apply to stakeholders using classic principles. The principles are: (1) utilitarianism, (2) universalism, (3) rights, (4) justice, and (5) ethical virtue. After reviewing these principles, we show some "quick ethical tests" that can also be used to clarify ethical dilemmas.

Take the quick ethics assessment in Ethical Insight 2.1. After you have read and reflected on the five principles, return to the assessment and see which of the principles you may consciously or routinely use in your everyday decision making or when deciding complex dilemmas. Which principle would "work" for you?

Ethical Insight 2.1

Are You Ethical?

Answer each question with your first reaction. Circle the number, from 1 to 4, that best represents your beliefs, if 1 represents "Completely agree," 2 represents "Often agree," 3 represents "Somewhat disagree," and 4 represents "Completely disagree."

1. I consider myself the type of person who does whatever it takes to get the job done, period. 1 2 3 4
2. Ethics should be taught at home and in the family, not in professional or higher education. 1 2 3 4
3. I believe that the "golden rule" is that the person who has the gold rules. 1 2 3 4
4. Rules are for people who don't really want to make it to the top of a company. 1 2 3 4
5. Acting ethically at home and with friends is not the same as acting ethically on the job. 1 2 3 4
6. I would do what is needed to promote my own career in a company, short of committing a serious crime. 1 2 3 4
7. Cutthroat competition is part of getting ahead in the business world. 1 2 3 4
8. Lying is usually necessary to succeed in business. 1 2 3 4
9. I would hide truthful information about someone or something at work to save my job. 1 2 3 4
10. I consider money to be the most important reason for working at a job or in an organization. 1 2 3 4

Add up all the points. Your Total Score is: _____

Total your scores by adding up the numbers you circled. The lower your score, the more questionable your (business-related) ethical principles. The lowest possible score is 10, which indicates you are highly unethical; the highest score is 40, indicating you are highly ethical; 20 signals "questionable ethics"; 30 indicates you are more ethical than unethical, but caution should be taken about consequences of your behaviors.

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Utilitarianism: A Consequentialist (Results-Based) Approach

Jeremy Bentham (1748–1832) and John Stuart Mill (1806–1873) are acknowledged as founders of the concept of *utilitarianism.* Although various interpretations of the concept exist, the basic utilitarian view holds that an action is judged as right or good on the basis of its consequences. The ends of an action justify the means taken to reach those ends. As a *consequentialist principle,* the moral

authority that drives utilitarianism is the calculated *consequences,* or results, of an action, regardless of other principles that determine the means or motivations for taking the action. Utilitarianism also includes the following tenets:[5]

1. An action is morally right if it produces the greatest good for the greatest number of people.
2. An action is morally right if the net benefits over costs are greatest for all affected, compared with the net benefits of all other possible choices.
3. An action is morally right if its benefits are greatest for each individual and if these benefits outweigh the costs and benefits of the alternatives.

There are also two types of criteria used in utilitarianism: *rule*-based and *act*-based.[6, 7] Rule-based utilitarianism argues that general principles are used as criteria for deciding the greatest benefit to be achieved from acting a certain way. The act itself is not the basis used for examining whether the greatest good can be gained. For example, "stealing is not acceptable" could be a principle that rule-based utilitarians would follow to gain the greatest utility from acting a certain way. "Stealing is not acceptable" is not an absolute principle that rule-based utilitarians would follow in every situation. Rule-based utilitarians might choose another principle over "stealing is not acceptable" if the other principle provided a greater good.

Act-based utilitarians, on the other hand, analyze a particular action or behavior to determine whether the greatest utility or good can be achieved. Act-based utilitarians might also choose an action over a principle if the greatest utility could be gained. For example, an employee might reason that illegally removing an untested chemical substance from company storage would save the lives of hundreds of infants in a less advantaged country because that chemical is being used in an infant formula manufactured in that country. The employee could lose his job if caught; still he calculates that stealing the chemical in this situation provides the greatest utility.

Utilitarian concepts are widely practiced by government policy makers, economists, and business professionals. Utilitarianism is a useful principle for conducting a stakeholder analysis, because it forces decision makers to (1) consider collective as well as particular interests, (2) formulate alternatives based on the greatest good for all parties involved in a decision, and (3) estimate the costs and benefits of alternatives for the affected groups.[8]

Louise Simms could use utilitarian principles in her decision making by identifying each of the stakeholders who would be affected by her decision. She would then calculate the costs and benefits of her decision as they affect each group. Finally, she would decide on a course of action based on the greatest good for the greatest number. For example, after identifying all the stakeholders in her decision, including her own interests, Simms might believe that her firm's capabilities were not competitive and that rejecting the offer would produce the greatest good for the people of the country where the contract would be negotiated, because obtaining bids from the most technically qualified companies would best serve the interests of those receiving the services.

Problems with utilitarianism include the following:

1. No agreement exists about the definition of "good" for all concerned. Is it truth, health, peace, profits, pleasure, cost reductions, or national security?[9]
2. No agreement exists about who decides. Who decides what is good for whom? Whose interests are primary in the decisions?
3. The actions are not judged, but rather their consequences. What if some actions are simply wrong? Should decision makers proceed to take those actions based only on their consequences?
4. How are the costs and benefits of nonmonetary stakes, such as health, safety, and public welfare, measured? Should a monetary value be assigned to nonmarketed benefits and costs?[10] What if the actual or even potentially harmful effects of an action cannot be measured in the short term, but the action is believed to have potentially long-term effects, say in 20 or 30 years? Should that action be chosen?
5. Utilitarianism does not consider the individual. It is the collective for whom the greatest good is estimated. Do instances exist when individuals and their interests should be valued in a decision?
6. The principles of justice and rights are ignored in utilitarianism. The principle of justice is concerned with the distribution of good, not the amount of total good in a decision. The principle of rights is concerned with individual entitlements, regardless of the collective calculated benefits.

Even given these problems, the principle of utilitarianism is still valuable under some conditions: when resources are fixed or scarce; when priorities are in conflict; when no clear choice fulfills everyone's needs; and when large or diverse collectives are involved in a zero-sum decision, that is, when a gain for some corresponds to a loss for others.[11]

Utilitarianism and Stakeholder Analysis

Because businesses use utilitarian principles when conducting a stakeholder analysis, you, as a decision maker, should:

1. Define how costs and benefits will be measured in selecting one course of action over another—including social, economic, and monetary costs and benefits as well as long-term and short-term costs and benefits. On what principle, if any, would you use to base your utilitarian analysis?
2. Define what information you will need to determine the costs and benefits for comparisons.
3. Identify the procedures and policies you will use to explain and justify your cost-benefit analysis.
4. State your assumptions when defining and justifying your analysis and conclusions.
5. Ask yourself what moral obligations you have toward each of your stakeholders after the costs and benefits have been estimated.

Universalism: A Deontological (Duty-Based) Approach

Immanuel Kant (1724–1804) is considered one of the leading founders of the principle of *universalism*. Universalism, which is also called deontological ethics, holds that the ends do not justify the means of an action—the right thing must always be done, even if doing the wrong thing would do the most good for the most people. Universalism, therefore, is also referred to as a *nonconsequentialist* ethic. The term "deontology" is derived from the Greek word *deon,* or duty. Regardless of consequences, this approach is based on universal principles, such as justice, rights, fairness, honesty, and respect.[12]

Kant's principle of the *categorical imperative*, unlike utilitarianism, places the moral authority for taking action on an individual's duty toward other individuals and "humanity." The categorical imperative consists of two parts. The first part states that *a person should choose to act if and only if she or he would be willing to have every person on earth, in that same situation, act exactly that way.* This principle is absolute and allows for no qualifications across situations or circumstances. The second part of the categorical imperative states that, in an ethical dilemma, *a person should act in a way that respects and treats all others involved as ends as well as means to an end*.[13]

Kant's categorical imperative forces decision makers to take into account their duty to act responsibly and respectfully toward all individuals in a situation. Individual human welfare is a primary stake in any decision. Decision makers must also consider formulating their justifications as principles to be applied to everyone.

In Louise Simms's situation, if she followed deontological principles of universalism, she might ask, "If I accept the official's offer, could I justify that anyone anywhere would act the same way?" Or, "Since I value my own self-respect and believe my duty is to uphold self-respect for others, I will not accept this assignment because my self-respect has been and may again be violated."

The major weaknesses of universalism and Kant's categorical imperative include these criticisms: First, these principles are imprecise and lack practical utility. It is difficult to think of all humanity each time one must make a decision in an ethical dilemma. Second, it is hard to resolve conflicts of interest when using a criterion that states that all individuals must be treated equally. Degrees of differences in stakeholders' interests and relative power exist. However, Kant would remind us that the human being and his or her humanity must be considered above the stakes, power bases, or consequences of our actions. Still, it is often impractical not to consider other elements in a dilemma. Finally, what if a decision maker's duties conflict in an ethical dilemma? The categorical imperative does not allow for prioritizing. A primary purpose of the stakeholder analysis is to prioritize conflicting duties. It is, again, difficult to take absolute positions when limited resources and time and conflicting values are factors.

Universalism and Stakeholder Analysis

The logic underlying universalism and the categorical imperative can be helpful for applying a stakeholder analysis. Even though we may not be able

to employ Kant's principles absolutely, we can consider the following as guidelines for using his ethics:

1. Take into account the welfare and risks of all parties when considering policy decisions and outcomes.
2. Identify the needs of individuals involved in a decision, the choices they have, and the information they need to protect their welfare.
3. Identify any manipulation, force, coercion, or deceit that might harm individuals involved in a decision.
4. Recognize the duties of respecting and responding to individuals affected by particular decisions before adopting policies and actions that affect them.
5. Ask if the desired action would be acceptable to the individuals involved. Under what conditions would they accept the decision?
6. Ask if individuals in a similar situation would repeat the designated action or policy as a principle. If not, why not? And would they continue to employ the designated action?

Rights: A Moral and Legal Entitlement-Based Approach

Rights are based on several sources of authority.[14] *Legal rights* are entitlements that are limited to a particular legal system and jurisdiction. In the United States, the Constitution and Declaration of Independence are the basis for citizens' legal rights, for example the right to life, liberty, and the pursuit of happiness, and the right to freedom of speech. *Moral* (and *human*) *rights*, on the other hand, are universal and based on norms in every society, for example, the right not to be enslaved and the right to work.

Moral and legal rights are linked to individuals, and in some cases, groups, not to societies, as is the case with a utilitarian ethic. Moral rights are also connected with duties, that is, my moral rights imply that others have a duty toward me to not violate those rights, and vice versa. Moral rights also provide the freedom to pursue one's interests, as long as those interests do not violate others' rights. Moral rights also allow individuals to justify their actions and seek protection from others in doing so.

There are also special rights and duties, or *contractual rights*. Contracts provide individuals with mutually binding duties that are based on a legal system with defined transactions and boundaries. Moral rules that apply to contracts include: (1) the contract should not commit the parties to unethical or immoral conduct; (2) both parties should freely and without force enter the contractual agreement; (3) neither individual should misrepresent or misinterpret facts in the contract; and (4) both individuals should have complete knowledge of the nature of the contract and its terms before they are bound by it.[15]

Finally, the concept of *negative* and *positive rights* defines yet another dimension of ethical principles.[16] A *negative right* refers to the duty others have to not interfere with actions related to a person's rights. For example, if you have the right to freedom of speech, others—including your employer—have

the duty not to interfere with that right. Of course there are circumstances that constrain "free speech," which we will discuss in Chapter 4. A *positive right* imposes a duty on others to provide for your needs to achieve your goals, not just protect your right to pursue them. Some of these rights may be part of national, state, or local legislation. For example, you may have the right to equal educational opportunities for your child if you are a parent. This implies that you have the right to send your child to a public school that has the same standards as any other school in your community.

Positive rights were given attention in the twentieth century. National legislation that promoted different groups' rights and the United Nations' Universal Declaration of Human Rights served as sources for positive rights. Negative rights were emphasized in the seventeenth and eighteenth centuries and were based on the Bill of Rights in the Declaration of Independence. Currently, American political parties and advocates who are either politically to the "left" or to the "right" debate on whether certain moral rights are "negative" or "positive" and to what extent taxpayers' dollars and government funds should support these rights. For example, "conservative" writers like Milton Friedman[17] have endorsed government support of negative rights (like protecting property, and enforcing law and order) and argued against public spending on positive rights (like medical assistance, job training, and housing). As you can see, the concept of rights has several sources of moral authority. Understanding and applying the concept of rights to stakeholders in business situations adds another dimension of ethical discovery to your analysis.

Louise Simms might ask what her rights are in her situation. If she believes that her constitutional and moral rights would be violated by accepting the offer, she would consider refusing to negotiate on the foreign official's terms.

The limitations of the principle of rights include:

1. The justification that individuals are entitled to rights can be used to disguise and manipulate selfish, unjust political claims and interests.
2. Protection of rights can exaggerate certain entitlements in society at the expense of others. Fairness and equity issues may be raised when the rights of an individual or group take precedence over the rights of others. Issues of reverse discrimination, for example, have arisen from this reasoning.
3. The limits of rights come into question. To what extent should practices that may benefit society, but threaten certain rights, be permitted?

Rights and Stakeholder Analysis

The principle of rights is particularly useful in stakeholder analysis when conflicting legal or moral rights of individuals occur or when rights may be violated if certain courses of action are pursued. The following are guidelines for observing this principle:[18]

1. Identify the individuals whose rights may be violated.
2. Determine the legal and moral bases of these individuals' rights. Does the decision violate these rights on such bases?

3. Determine to what extent the action has moral justification from utilitarian or other principles if individual rights may be violated. National crises and emergencies may warrant overriding individual rights for the public good.

Justice: Procedures, Compensation, and Retribution

The principle of *justice* deals with fairness and equality. Here, the moral authority that decides what is right and wrong concerns the fair distribution of opportunities, as well as hardships, to all. The principle of justice also pertains to punishment for wrong done to the undeserving. John Rawls, a contemporary philosopher, offers two principles of fairness that are widely recognized as representative of the principle of justice:[19]

1. Each person has an equal right to the most extensive basic liberties that are compatible with similar liberties for others.
2. Social and economic inequalities are arranged so that they are both (a) reasonably expected to be to everyone's advantage and (b) attached to positions and offices open to all.

The first principle states that all individuals should be treated equally. The second principle states that justice is served when all persons have equal opportunities and advantages (through their positions and offices) to society's opportunities and burdens. Equal opportunity or access to opportunity does not guarantee equal distribution of wealth. Society's disadvantaged may not be justly treated, some critics claim, when only equal opportunity is offered. The principle of justice also addresses the unfair distribution of wealth and the infliction of harm.

Richard DeGeorge identifies four types of justice:[20]

1. *Compensatory justice* concerns compensating someone for a past harm or injustice. For example, affirmative action programs, discussed in Chapter 7, are justified, in part, as compensation for decades of injustice that minorities have suffered.
2. *Retributive justice* means serving punishment to someone who has inflicted harm on another. A criterion for applying this justice principle is: "Does the punishment fit the crime?"
3. *Distributive justice* refers to the fair distribution of benefits and burdens. Have certain stakeholders received an unfair share of costs accompanying a policy or action? Have others unfairly profited from a policy?
4. *Procedural justice* designates fair decision practices, procedures, and agreements among parties. This criterion asks, "Have the rules and processes that govern the distribution of rewards, punishments, benefits, and costs been fair?"

These four types of justice are part of the larger principle of justice. How they are formulated and applied varies with societies and governmental systems.

Following the principle of justice, Louise Simms might ask whether accepting the government official's offer would provide a fair distribution of goods and services to the recipients of the new technological system. Also, are the conditions demanded by the government administrator fair for all parties concerned? If Simms determined that justice would not be served by enabling her company to be awarded the contract without a fair bidding process, she might well recommend that her firm reject the offer.

The obvious practical problems of using the principle of justice include the following: Outside the jurisdiction of the state and its judicial systems, where ethical dilemmas are solved by procedure and law, who decides who is right and who is wrong? Who has the moral authority to punish whom? Can opportunities and burdens be fairly distributed to all when it is not in the interest of those in power to do so?

Even with these shortcomings, the principle of justice adds an essential contribution to the other ethical principles discussed so far. Beyond the utilitarian calculation of moral responsibility based on consequences, beyond the universalist absolute duty to treat everyone as a means and not an end, and beyond the principle of rights, which values unquestionable claims, the principle of justice forces us to ask how fairly benefits and costs are distributed, regardless of power, position, or wealth.

Rights, Power, and "Transforming Justice"

Justice, rights, and power are really intertwined. Rights plus power equals "transforming justice." T. McMahon states, "While natural rights are the basis for justice, rights cannot be realized nor justice become operative without power."[21] Judges and juries exercise power when two opposing parties, both of whom are "right," seek justice from the courts.

Power generally is defined and exercised through inheritance, authority, contracts, competition, manipulation, and force. Power exercised through manipulation cannot be used to obtain justice legitimately. The two steps in exercising "transforming justice" are:

1. Be aware of your rights and power. McMahon states, "It is important to determine what rights and how much legitimate power are necessary to exercise these rights without trampling on other rights. For example, an employer might have the right and the power to fire an insolent employee, but she or he might not have enough to challenge union regulations."[22]

2. Establish legitimate power as a means for obtaining and establishing rights. According to McMahon, "If the legitimacy of transforming justice cannot be established, its exercise may then be reduced to spurious power plays to get what someone wants, rather than a means of fulfilling rights."[23]

3. This interrelationship of rights, justice, and power is particularly helpful in studying stakeholder management relationships. Since stakeholders exercise power to implement their interests, the concept of "rights plus power equals transforming justice" adds value in determining justice (procedural, compensatory, and retributive). The question of justice in complex, competitive

situations becomes not only "Whose rights are more right?" but also "By what means and to what end was power exercised?"

Justice and Stakeholder Analysis

In a stakeholder analysis, the principle of justice can be applied by asking the following questions:

1. How equitable will the distribution of benefits and costs, pleasure and pain, and reward and punishment be among stakeholders if you pursue a particular course of action? Would all stakeholders' self-respect be acknowledged?

2. How clearly have the procedures for distributing the costs and benefits of a course of action or policy been defined and communicated? How fair are these procedures to all affected?

3. What provisions can be made to compensate those who will be unfairly affected by the costs of the decision? What provisions can we make to redistribute benefits among those who have been unfairly or overly compensated by the decision?

Virtue Ethics: Character-Based Virtues

Plato and Aristotle are recognized as founders of virtue ethics, which also has roots in ancient Chinese and Greek philosophy. Virtue ethics emphasizes moral character in contrast to moral rules (deontology) or consequences of actions (consequentialism).[24]

Virtue ethics is grounded in "character traits," that is, "a disposition which is well entrenched in its possessor, something that, as we say 'goes all the way down', unlike a habit such as being a tea-drinker—but the disposition in question, far from being a single track disposition to do honest actions, or even honest actions for certain reasons, is multi-track. It is concerned with many other actions as well, with emotions and emotional reactions, choices, values, desires, perceptions, attitudes, interests, expectations and sensibilities. To possess a virtue is to be a certain sort of person with a certain complex mindset. (Hence the extreme recklessness of attributing a virtue on the basis of a single action.)"[25]

The concepts of virtue ethics derived from ancient Greek philosophy are the following: virtue, practical wisdom, and eudaemonia (or happiness, flourishing, and well-being). Virtue ethics focuses on the type of person we ought to be, not on specific actions that should be taken. It is grounded in good character, motives, and core values. Virtue ethics argue that the possessor of good character is and acts moral, feels good, is happy, and flourishes. Practical wisdom, however, is often required to be virtuous. Adults can be culpable in their intentions and actions by being "thoughtless, insensitive, reckless, impulsive, shortsighted, and by assuming that what suits them will suit everyone instead of taking a more objective viewpoint. They are also, importantly, culpable if their understanding of what is beneficial and harmful is mistaken. It is part of practical wisdom to know how to secure real benefits effectively; those who have practical wisdom will not make the mistake of concealing

the hurtful truth from the person who really needs to know it in the belief that they are benefiting him."[26]

Critiques of virtue ethics include the following major arguments:

> First, virtue ethics fails to adequately address dilemmas which arise in applied ethics, such as abortion. For, virtue theory is not designed to offer precise guidelines of obligation. Second, virtue theory cannot correctly assess the occasional tragic actions of virtuous people. . . . Since virtue theory focuses on the general notion of a good person, it has little to say about particular tragic acts. Third, some acts are so intolerable, such as murder, that we must devise a special list of offenses which are prohibited. Virtue theory does not provide such a list. Fourth, character traits change, and unless we stay in practice, we risk losing our proficiency in these areas. This suggests a need for a more character-free way of assessing our conduct. Finally, there is the problem of moral backsliding. Since virtue theory emphasizes long-term characteristics, this runs the risk of overlooking particular lies, or acts of selfishness, on the grounds that such acts are temporary aberrations.[27]

These same criticisms also apply to other ethical principles and schools of thought.

Virtue Ethics and Stakeholder Analysis

Virtue ethics adds an important dimension to rules and consequentialist ethics by contributing a different perspective for understanding and executing stakeholder management. Examining the motives and character of stakeholders can be helpful in discovering underlying motivations of strategies, actions, and outcomes in complex business and corporate transactions. With regard to corporate scandals, virtue ethics can explain some of the motives of several corporate officers' actions that center on greed, extravagant habits, irrational thinking, and egotistical character traits.

Virtue ethics also adds a practical perspective. Beauchamp and Childress state, "A practical consequence of this view is that the education of, for example medical doctors, should include the cultivation of virtues such as compassion, discernment, trustworthiness, integrity, conscientiousness as well as benevolence (desire to help) and nonmalevolence (desire to avoid harm)."[28] These authors also note that "persons of 'good character' can certainly formulate 'bad policy' or make a 'poor choice'—we need to evaluate those policies and choices according to moral principles."

The Common Good

Plato and Aristotle are believed to be the authors of the common good concept. The ethicist John Rawls has developed and redefined the notion of the *common good* as "certain general conditions that are . . . equally to everyone's advantage."[29] The common good has also been defined as "the sum of those conditions of social life which allow social groups and their individual members relatively thorough and ready access to their own fulfillment."[30] The

common good includes the broader interdependent institutions, social systems, environments, and services and goods. Examples of the common good include the health care system, legislative and judicial systems, political, economic, and legal systems, and the physical environment. These systems exist at the local, regional, national, and global levels. Individuals, groups, and populations are dependent on these interlocking systems.[31] The common good must be created and maintained in societies. Cooperative and collaborative effort is required. "The common good is a good to which all members of society have access, and from whose enjoyment no one can be easily excluded. All persons, for example, enjoy the benefits of clean air or an unpolluted environment, or any of our society's other common goods. In fact, something counts as a common good only to the extent that it is a good to which all have access."[32]

The ethic of the common good suggests that decision makers take into consideration the intent as well as the effects of their actions and decisions on the broader society and the common good of the many. There are four major constraining factors and arguments on the notion of the common good: (1) A unitary notion of the common good is not viable in a pluralistic society. The common good means different things to different people. (2) Relatedly, in an individualistic society, people are rewarded to provide and succeed by themselves. The logic of the common good runs counter in many instances to this individualist cultural orientation. (3) "Free riders" abuse the provision of the common good by taking advantage of the benefits, while not contributing to the upkeep of common goods. A critical mass of free riders can and does destroy common goods, such as parts of the environment. (4) Finally, helping create and sustain common goods means unequal sharing of burdens and sacrifices by some groups, since not all groups will exert such efforts. Expecting some groups to support the common good while others will not is unjust, and perhaps impractical. Given these obstacles, the ethic of the common good calls us to share in a common vision of a society that benefits and is beneficial for all members, while respecting individual differences. Using this ethic in our decision making also calls us to take goals and actions that include others besides ourselves and our own interest into account. Such a logic is not just partly altruistic, but, in many circumstances, practical. We thrive when we breathe clean air, drink clean water, and can trust that the food we eat is not contaminated. This logic may also apply to business decisions that involve our customers and employees, as well as our neighbors, family members, and ourselves as members of a society as well as an organization. By using this principle, Louise would consider what good would be gained from actions taken not only for the professionals involved in her company and the client's, but also for the host society. She would have to evaluate ethical principles that serve the common good and benefits of the people in that country.

Ethical Relativism: A Self-Interest Approach

Ethical relativism holds that no universal standards or rules can be used to guide or evaluate the morality of an act. This view argues that people set their own moral standards for judging their actions. Only the individual's self-interest

and values are relevant for judging his or her behavior. This form of relativism is also referred to as *naive relativism*.

Individuals, professionals, and organizations using this approach can consider finding out what the industry and/or professional standard or norm is with regard to an issue. Another suggestion would be to inflict no undue harm with a course of action taken.[33]

If Louise Simms were to adopt the principle of ethical relativism for her decision making, she might choose to accept the government official's offer to promote her own standing in his firm. She might reason that her self-interest would be served best by making any deal that would push her career ahead. But Simms could also use ethical relativism to justify her rejection of the offer. She might say that any possible form of such a questionable negotiation is against her beliefs. The point behind this principle is that individual standards are the basis of moral authority.

The logic of ethical relativism also extends to cultures. *Cultural relativism* argues that "when in Rome, do as the Romans do." What is morally right for one society or culture may be wrong for another. Moral standards vary from one culture to another. Cultural relativists would argue that firms and business professionals doing business in a country are obliged to follow that country's laws and moral codes. A criterion that relativists would use to justify their actions would be: "Are my beliefs, moral standards, and customs satisfied with this action or outcome?"

The benefit of ethical and cultural relativism is that they recognize the distinction between individual and social values and customs. These views take seriously the different belief systems of individuals and societies. Social norms and mores are seen in a cultural context.

However, relativism can lead to several problems. (It can be argued that this perspective is actually not ethical.) First, these views imply an underlying laziness.[34] Individuals who justify their morality only from their personal beliefs, without taking into consideration other ethical principles, may use the logic of relativism as an excuse for not having or developing moral standards. Second, this view contradicts everyday experience. Moral reasoning is developed from conversation, interaction, and argument. What I believe or perceive as "facts" in a situation may or may not be accurate. How can I validate or disprove my ethical reasoning if I do not communicate, share, and remain open to changing my own standards?

Ethical relativism can create absolutists—individuals who claim their moral standards are right regardless of whether others view the standards as right or wrong. For example, what if my beliefs conflict with yours? Whose relativism is right then? Who decides and on what grounds? In practice, ethical relativism does not effectively or efficiently solve complicated conflicts that involve many parties because these situations require tolerating doubts and permitting our observations and beliefs to be informed.

Cultural relativism embodies the same problems as ethical relativism. Although the values and moral customs of all cultures should be observed and respected, especially because business professionals are increasingly operating across national boundaries, we must not be blindly absolute or divorce

ourselves from rigorous moral reasoning or laws aimed at protecting individual rights and justice. For example, R. Edward Freeman and Daniel Gilbert Jr. ask, "Must American managers in Saudi Arabia treat women as the Saudis treat them? Should Saudis in the U.S. treat women as they do in Saudi Arabia? Must American managers in South Africa [during the apartheid years] treat blacks as white South Africans treat them? Must white South Africans treat blacks in the United States as U.S. managers treat them? Must Saudis in the United States treat women as U.S. managers treat them?"[35] They continue, "It makes sense to question whether the norms of the Nazi society were in fact morally correct."[36] Using rigorous ethical reasoning to solve moral dilemmas is important across cultures.

However, this does not suggest that flexibility, sensitivity, and awareness of individual and cultural moral differences are not necessary. It does mean that upholding principles of rights, justice, and freedom in some situations may conflict with the other person's or culture's belief system. Depending on the actions taken and decisions made based on a person's moral standards, a price may be paid for maintaining them. Often, negotiation agreements and understanding can be reached without overt conflict when different ethical principles or cultural standards clash.

Finally, it could be argued that cultural relativism does provide an argument against cultural imperialism. Why should American laws, customs, and values that are embedded in a U.S. firm's policies be enforced in another country that has differing laws and values regarding the activities in question?

Ethical Relativism and Stakeholder Analysis

When considering the perspectives of relativism in a stakeholder analysis, ask the following questions:

1. What are the major moral beliefs and principles at issue for each stakeholder affected by this decision?
2. What are my moral beliefs and principles in this decision?
3. To what extent will my ethical principles clash if a particular course of action is taken? Why?
4. How can conflicting moral beliefs be avoided or resolved in seeking a desirable outcome?
5. What is the industry standard and norm with regard to this issue(s)?

A now classic case of the example of ethical relativism is Samuel Waksal, who resigned as chief executive officer (CEO) of ImClone (a manufacturer of drugs for cancer and other treatment therapies) on May 22, 2002. He was later arrested and indicted for bank fraud, securities fraud, and perjury. He pleaded guilty to all of the counts in the indictment. (He also implicated his daughter and father in his insider-trading schemes.) In addition, he pleaded guilty to tax evasion for not paying New York state sales tax on pieces of art that he had purchased. He was sentenced to 87 months in prison and was ordered to pay a $3 million fine and $1.2 million in restitution to the New York State Sales Tax Commission. He began serving his prison sentence on

July 23, 2003. Martha Stewart, an ImClone stockholder, was sentenced to five months in prison and five months of house arrest for using insider trading knowledge to sell shares of ImClone stock. She was also ordered to pay $30,000 in fines and court fees. Her broker, Peter Bacanovic, was given the same sentence, but a lower fine of $4,000. Bacanovic's assistant, Douglas Faneuil, was spared prison time and fined $2,000.[37] When asked in an interview how he got into this "mess," Waksal said, "It certainly wasn't because I thought about it carefully ahead of time. I think I was arrogant enough at the time to believe that I could cut corners, not care about details that were going on, and not think about consequences."[38]

Immoral, Amoral, and Moral Management

In addition to the classic ethical principles, three broad, straight moral orientations that can be applied to individuals, groups, and organizations are: immorality, amorality, and morality.

Immoral management of employees, stakeholders, and constituencies signifies a minimally ethical or unethical approach, such as laying off employees without fair notice or compensation, offering upper-level management undeserved salary increases and perks, and giving "golden parachutes" (attractive payments or settlement contracts to selected employees) when a change in company control is negotiated. (Such payments are often made at the expense of shareholders' dividends without their knowledge or consent.) Managing immorally means intentionally going against the ethical principles of justice and fair and equitable treatment of other stakeholders.

Amoral management happens when owners, supervisors, and managers treat shareholders, outside stakeholders, and employees without concern or care for the consequences of their actions. No willful wrong may be intended, but neither is thought given to moral behavior or outcomes. Minimal action is taken while setting policies that are solely profit-oriented, production-centered, or short-term. Employees and other stakeholders are viewed as instruments for executing the economic interests of the firm. Strategies, control systems, leadership style, and interactions in such organizations also reflect an amoral, minimalist approach toward stakeholders. Nevertheless, the harmful consequences of amoral actions are real for the persons affected.

Moral management places value on fair treatment of shareholders, employees, customers, and other stakeholders. Ethics codes are established, communicated, and included in training; employee rights are built into visible policies that are enforced; and employees and other stakeholders are treated with respect and trust. The firm's corporate strategy, control and incentive systems, leadership style, and interactions reflect a morally managed organization. Moral management is the preferred mode of acting toward stakeholders, since respect and fairness are considered in decisions.

It is helpful to consider these three orientations while observing managers, owners, employees, and coworkers. Have you seen amoral policies, procedures, and decisions in organizations? The next section summarizes four social responsibility roles that business executives view as moral for decision

makers. The model presented complements the five ethical principles by providing a broad framework for describing ethical orientations toward business decisions. You can also use the following framework to characterize your own moral and responsible roles, those of your boss and colleagues, and even those of contemporary international figures in government or business.

2.3 Four Social Responsibility Roles

What social obligations do businesses and their executives have toward their stockholders and society? The traditional view that the responsibility of corporate owners and managers is to serve only, or primarily, their stockholders' interests has been challenged and modified—but not abandoned—since the turn of this century. The debate continues about whether the roles of businesses and managers include serving social stakeholders along with economic stockholders. Because of changing demographic and educational characteristics of the workplace and the advent of laws, policies, and procedures that recognize greater awareness of employee and other stakeholders' rights, distinctions have been made about the responsibility of the business to its employees and to the larger society.

Four ethical interpretations of the social roles and modes of decision making are discussed and illustrated in Figure 2.2. The four social responsibility modes reflect business roles toward stockholders and a wider audience of stakeholders.[39]

Notice the two distinct social responsibility orientations of businesses and managers toward society: the *stockholder model* (the primary responsibility of the corporation to its economic stockholders) and the *stakeholder model* (the responsibility of the corporation to its social stakeholders outside the corporation). The two sets of motives underlying these two orientations are "self-interest" and "moral duty."

The stockholder self-interest (cell 1 in Figure 2.2) and moral duty (cell 3) orientations are discussed first, followed by the stakeholder self-interest (cell 2)

Figure 2.2

Four Social Responsibility Modes and Roles

		ORIENTATIONS	
		Stockholder Model	Stakeholder Model
MOTIVES	Self-Interest	1 Productivism	2 Progressivism
	Moral Duty	3 Philanthropy	4 Ethical Idealism

Source: Buono, Anthony F., and Nicholas, Lawrence. (1990). Stockholder and stakeholder interpretations of business' social role. In Michael Hoffman and Jennifer Moore (eds.), *Business ethics: Readings and cases in corporate morality,* 2nd ed., 172. New York: McGraw-Hill. Reproduced with the permission of Anthony F. Buono.

and moral duty (cell 4) orientations. The two stockholder orientations are productivism and philanthropy.

Productivists (who hold a free-market ethic) view the corporation's social responsibility in terms of rational self-interest and the direct fulfillment of stockholder interests. The free market values the basis of rewards and punishments in the organization. This ethic drives internal and external vision, mission, values, policies, and decisions—including salaries, promotion, and demotions. Productivists believe the major—and, some would say, only—mission of business is to obtain profit. The free market is the best guarantee of moral corporate conduct in this view. Supply-side economists as productivists, for example, argue that the private sector is the vehicle for social improvement. Tax reduction and economic incentives that boost private industry are policies that productivists advocate as socially responsible. Former President George W. Bush's initial response to the subprime lending crisis exemplifies a productivist approach; as BBC News reported, Bush's efforts included "reform tax laws to help troubled borrowers refinance their loans, but the President added that it was not the government's job to bail out speculators."[40] President Bush eased that position as the U.S. and global economies approached a near collapse. U.S. presidents must make policy decisions that balance all these responsibility modes, while being very concerned about stakeholders, many of whom are the public citizenry.

Although all the ethical principles discussed earlier could be used by organizational leaders within each of these responsibility modes, productivists might find themselves advocating the use of *negative rights* to promote policies that protect shareholders' interests over positive rights that would cost taxpayers and use government resources to assist those more economically dependent on government services—who, productivists would argue, add an economic burden to the free-market system.

A free-market-based ethic is widely used by owners and managers who must make tough workplace decisions, such as: (1) How many and which people are to be laid off because of a market downturn and significantly lower profits? (2) What constitutes fair notice and compensation to employees who are to be terminated from employment? (3) How can employees be disciplined fairly in situations in which people's rights have been violated? A company is entitled to private property rights and responsibilities to shareholders. Robert Nozick, a libertarian philosopher, is an advocate of a market-based ethic. He makes a case for a market-based principle of justice and entitlement in his classic book *Anarchy, State, and Utopia*. Opponents of the market-based ethic argue that the rights of less advantaged people also count; that property rights are not absolute in all situations; that there are times when the state can be justified in protecting the rights of others in disputes against property owners; and that the distribution of justice depends on the conditions of a situation—if war, illegal entry, fraud, or theft occur, some form of redistribution of wealth can be justified.[41]

Philanthropists, who also have a stockholder view of the corporation, hold that social responsibility is justified in terms of a moral duty toward helping less advantaged members of society through organized, tax-deductible charity

and *stewardship*. Proponents of this view believe that the primary social role of the corporation is still to obtain profits. However, moral duty drives their motives instead of self-interest (the productivist view). Advocates of this view are stewards and believe that those who have wealth ought to share it with disadvantaged people. As stockholder stewards, philanthropists share profits primarily through their tax-deductible activities. Warren Buffett gave 85% of his wealth, estimated over $44 billion, to philanthropic causes, including the Bill & Melinda Gates Foundation. The remainder will be given to foundations operated by his children.[42]

Philanthropists might argue from principles of utilitarianism, duty, and universalism to justify their giving. Corporate philanthropy, generally speaking, is based primarily on the profit motive. Corporate philanthropists' sense of stewardship is contingent on their available and calculated use of wealth to help the less economically advantaged.

Progressivism and *ethical idealism* are the two social responsibility modes in the stakeholder model, the other dominant orientation. *Progressivists* believe corporate behavior is motivated by self-interest, but they also hold that corporations should take a broader view of responsibility toward social change. The Pope might be considered an ethical idealist. Enlightened self-interest is a value that also characterizes progressivists. The renowned theologian Reinhold Niebuhr is a modern example of a progressivist who argued for the involvement of the church in politics to bring about reasoned, orderly reform. He also worked with unions and other groups to improve workers' job conditions and wages. Progressivists support policies such as affirmative action, environmental protection, employee stock option programs (ESOPs), and energy conservation. Did ice cream makers Ben Cohen and Jerry Greenfield, for example, follow a progressivist philosophy for their formerly independent company?

Finally, *ethical idealists* believe that social responsibility is justified when corporate behavior directly supports stakeholder interests. Ethical idealists, such as Ralph Nader earlier in his career, hold that, to be fully responsible, corporate activity should help transform businesses into institutions where workers can realize their full potential. Employee ownership, cooperatives, and community-based and owned service industries are examples of the type of corporate transformation that ethical idealists advocate. The boundaries between business and society are fluid for ethical idealists. Corporate profits are to be shared for humanitarian purposes—to help bring about a more humane society.

Of course, as noted previously, a spectrum of beliefs exists for each of these four modes. For example, ethical idealists profess different visions regarding the obligations of business to society. Progressivists and ethical idealists generally tend to base their moral authority on legal and moral rights, justice, and universalism. Organizational leaders and professionals are obviously concerned with the operational solvency and even profitability (especially for-profit firms) of their companies. Still, they tend to believe that stakeholder interests and welfare are necessary parts of the economic system's effectiveness and success.

Which orientation best characterizes your current beliefs of business responsibility toward society: productivism, philanthropy, progressivism, or ethical idealism? Keep in mind the ethical decision frameworks presented above and also your ethical assessment scores, as we turn to the different levels of ethical decision making.

2.4 Levels of Ethical Reasoning and Moral Decision Making

Understanding the nature of an ethical dilemma, the source and whom it is affecting are important steps toward responding. In this section, three levels or dimensions of ethical dilemmas are described in order to guard against "short-sightedness" when experiencing or analyzing an ethical dilemma.

Many ethical issues and dilemmas result from *pressures* that are experienced at four levels: (1) the personal level, (2) the company or organizational level, (3) the industry level, and (4) the societal, international, and global levels.

Personal Level

As the opening case of this chapter illustrates, a person experiences pressures from conflicting demands or circumstances that require a decision. Ethical dilemmas at this level can occur as a result of workplace pressures or from personal circumstances or motivations not related to work. Pressures on Louise stem from a supervisor's assignment, the consequences of which could affect others in the organization and possibly in the host culture. Is Louise being lied to? Is she being pressured to risk her integrity and even job or career by accepting this assignment? Note that what begins as an individual or personal dilemma can escalate into organizational and other levels, as is possible with Louise if the issues are not resolved.

Ethical dilemmas that do not start at the personal level can and do involve and affect individuals along the way. The personal focus on ethical decision making also involves a broader inquiry with regard to how do individual personalities, traits, maturity, and styles affect such decisions. For example, narcissism and cynicism are individual differences that influence self-perceptions and perceptions of others. Antes, et al. (2007) showed that these two traits in particular had a negative effect on aspects of ethical decision making, whereas basic personality characteristics, such as conscientiousness and agreeableness, did not have the same effect.[43] It sounds like common sense, but studies confirm—and sometimes dispute—what we think we already know. Similarly, Skarlicki, et al. (1999) also found that negative affectivity and agreeableness matter, in that these personality traits moderate the relationship between fairness perceptions and retaliation in the workplace.[44] McFerran, et al. (2010) found that moral personality and the centrality of moral identity were associated with a more principled (versus expedient) ethical ideology. That is, moral personality characteristics affect organizational citizenship behavior and the

propensity to morally disengage.[45] Ethical personality traits discussed here—agreeableness, conscientiousness, and a principled approach, as contrasted with negativity, narcissism, and cynicism—are associated with ethical activities in the workplace. These studies confirm that the principle of virtue ethics matters in organizational settings.

Moral maturity also matters. Kohlberg's three levels of moral development (which encompass six stages) provide a guide for observing our own and a person's level of moral maturity in everyday life and organizational settings. Whether, and to what extent, ethical education and training contribute to moral development in later years is not known. Most individuals in Kohlberg's 20-year study (limited to males) reached the fourth and fifth stages by adulthood. Only a few attained the sixth stage.

Level 1: Preconventional Level (Self-Orientation)

- Stage 1: Punishment avoidance: avoiding punishment by not breaking rules. The person has little awareness of others' needs.
- Stage 2: Reward seeking: acting to receive rewards for oneself. The person has awareness of others' needs but not of right and wrong as abstract concepts.

Level 2: Conventional Level (Others Orientation)

- Stage 3: Good person: acting "right" to be a "good person" and to be accepted by family and friends, not to fulfill any moral ideal.
- Stage 4: Law and order: acting "right" to comply with law and order and norms in societal institutions.

Level 3: Postconventional, Autonomous, or Principles Level (Universal, Humankind Orientation)

- Stage 5: Social contract: acting "right" to reach consensus by due process and agreement. The person is aware of relativity of values and tolerates differing views.
- Stage 6: Universal ethical principles: acting "right" according to universal, abstract principles of justice and rights. The person reasons and uses conscience and moral rules to guide actions.

Interestingly, one study of 219 corporate managers working in different companies found that managers typically reason at moral stage 3 or 4, which, the author notes, is "similar to most adults in the Western, urban societies or other business managers."[46] Managers in large- to medium-sized firms reasoned at lower moral stages than managers who were self-employed or who worked at small firms. Reasons offered for this difference in moral reasoning include that larger firms have more complex bureaucracies and layers of structure, more standard policies and procedures, and exert more rule-based control over employees. Employees tend to get isolated from other parts of the organization and feel less involved in the central decision-making process. On the other hand, self-employed professionals and managers in smaller firms tend to interact with people throughout the firm and with external stakeholders.

Involvement with and vulnerability to other stakeholders may cause these managers to adhere to social laws more closely and to reason at stage 4.

The same study also found that managers reasoned at a higher level when responding to a moral dilemma in which the main character was not a corporate employee. It could be that managers reason at a higher level when moral problems are not associated with the corporation. The author suggests that the influence of the corporation tends to restrict the manager to lower moral reasoning stages. Or it could be that the nature of the moral dilemma may affect the way managers reason (i.e., some dilemmas may be appropriately addressed with stage 3 or 4 reasoning, other dilemmas may require stage 5 logic).

Stephen Covey's "Moral Continuum" offers a developmental model for progressing from a basic state of dependence, to independence, and then interdependence using the "7 habits of highly effective people," which can be learned and practiced. The seven habits are: 1. Be Proactive, 2. Begin with the End in Mind, 3. Put First Things First, 4. Think Win–Win, 5. Seek First to Understand, Then to be Understood, 6. Synergize, and 7. Sharpen the Saw.

Breaking out of Dependency to Become Independent

Breaking out of dependency (less morally mature) to become more interdependent (highest level of moral maturity) is a process that involves the heart, mind, and body. According to Covey's Moral Continuum, once the first three habits are developed, a person builds character and a "Private Victory" is achieved. Developing and following the three habits signals a "Public Victory" on this moral journey. The first habit, "Be Proactive," embodies "the "Principle of Personal Vision," or taking control and being responsible for one's own life while acting with integrity. This means a person also begins to see how others see him/her, keeping commitments, and deciding to be oneself by developing a plan.[47] The second habit, "Begin with the End in Mind," embodies "the Principle of Personal Leadership," and involves a person's envisioning where she/he wishes to go in their life, answering what being successful means, and addressing what is really important. During this process, a person "re-scripts" their internalized messages and develops their own vision and goals, which entails them seeing the "big picture" around them and developing a "Personal Mission Statement," grounded in principles that matter most to them. The third habit, "Put First Things First," embodies the principle of "Personal Management," which involves implementing concrete plans only after a person believes that she or he will succeed. This habit helps a person refuse distractions and be able to delegate tasks to others to help the person reach their goals. Once these first three habits are achieved, a "Private Victory" from dependence has been accomplished.

From Independence to Interdependence

"Think Win–Win," the fourth habit, is based on the "Principle of Interpersonal Leadership," which involves building relationships through cooperation. A sense of integrity and maturity, and an abundance mentality are developed with this habit. The fifth habit, "Seek First to Understand, Then to be Understood" embodies the principle of "Emphatic Communication, which

involves communicating as an emphatic listener. Nonjudgmental listening builds goodwill in relationships. The sixth habit, "Synergize," embodies the "Principle of Creative Cooperation," and builds on the previous habits to form relationships that increase the work of two people beyond each individual's maximum efficiency. Synergy makes 1 + 1 = 3, that is, the results of two individuals working together is to equal the output of three or more individuals working independently. Flexibility, openness, and goodwill are part of this habit. Finally, the seventh habit, "Sharpen the Saw," which embodies the "Principle of Balanced Renewal" is based on the need for continuous self-renewal that requires physical, mental, and emotional effort to achieve life balance. Moral maturity is an ongoing process, not a destination.

With regard to this chapter's opening case and Louise's dilemma, the logic of the Moral Continuum, briefly summarized here, offers an opportunity of reflection for her to consider her personal values, mission, and character in deciding what course of action to follow or not to follow. Ethical decision making in serious dilemmas, or even those that may at first seem trivial, generally involves one's whole self.

Organizational Level

Firms that engage in questionable practices and activities face possible dilemmas with their stakeholders and/or stockholders. Studies show that when corporate values are dominated by financial profits, employees' ethical standards are diminished in their workplace decisions, as compared to corporations that value and reward integrity and good business practices.[48] For example, JPMorgan Chase's controversial CEO Jamie Dimon was recently found responsible for a host of mismanaged acts in 2012 that resulted in the following losses of that bank: a $6 billion trading fiasco named the London Whale; "a $4.3 billion settlement with federal and state prosecutors over mortgage abuses; a $297 million settlement with the Securities and Exchange Commission (SEC) over charges of lying to investors about the quality of mortgage-backed bonds; a $45 million settlement with the Department of Justice over charges of veterans' loan fraud; a cease-and-desist order for failures to comply with federal anti-money laundering laws; an ongoing federal investigation of LIBOR-rigging; a temporary ban on energy trading for failing to disclose information in a market manipulation investigation by the Federal Energy Regulatory Commission; accusations of manipulating silver prices."[49] Dimon's public statement over the London Whale loss was "Life goes on." JPMorgan's board of directors' response to Dimon's leadership while these questionable losses occurred was to halve his bonus to $10.5 million dollars. Dimon's leadership example brought public and regulatory attention to the type of ethical values and culture being practiced at JPMorgan, especially in the wake of the corporate scandals and crises experienced in the banking industry.

Or take the example of *Dukes v. Wal-Mart*. "The largest sexual discrimination lawsuit in U.S. history was brought against Wal-Mart when a federal appeals court approved class-action status for seven women who claim the

retailer was biased in pay and promotions."[50] Plaintiffs in that case estimated that 1.5 million women who had worked for Wal-Mart in the U.S. stores since 1998 were eligible to join that suit. Wal-Mart's reputation and image will not be easily repaired from this and other lawsuits that have recently been brought against the largest retailer. Going forward, Wal-Mart's officers must decide whether or not this type of possible discrimination is worth the legal, social, and media fallout for the company and its stakeholders.

Industry Level

Company officers, managers, and professionals working within and/or across industries may contribute to, and be influenced and affected by, specific business practices in an industry. A recent example of unethical and illegal industry-wide business practices is the 2007–2009 subprime mortgage lending crisis, in which some of the largest banks in the United States and other countries bundled asset-backed securities with real estate, including individuals' home mortgages, as collateral and then sold these to Wall Street investors. Such financial products were highly popular and promised huge returns, but they were bogus, and the result was a near global financial meltdown.

In this chapter's opening case, Louise can inquire about the business practice in which she is being pressured to engage (i.e., contract negotiations in a foreign country). She can explore whether or not such practices are legal in her company and industry. Even if she finds that such practices are used but are questionable ethically and legally, she will need to decide whether or not she wishes to assume personal liability and consequences of taking such actions.

Societal, International, and Global Levels

Industry, organizational, professional, and personal ethics may clash at the societal, global, and international levels. For example, although tipping and paying money to government and other business officials in some countries may meet local customary practices, such offerings may also be illegal bribes in other countries (like the United States and Europe). Chapter 8 addresses these types of issues.

In this chapter's opening case, Louise is walking a tightrope in her decision. She needs to consult the Foreign Corrupt Practices Act (discussed in Chapter 8) to determine whether or not her superiors are asking her personally and professionally—as a representative of her firm—to act illegally. She might also seek advice from someone in her company or in the country regarding cultural norms and business practices.

2.5 Identifying and Addressing Ethical Dilemmas

An ethical dilemma is a problem or issue that confronts a person, group, or organization and that requires a decision or choice among competing claims

and interests, all of which may be unethical (i.e., against all parties' principles). Decision choices presented by an ethical dilemma usually involve solutions that do not satisfy all stakeholders. In some situations, there may be a resolution to an ethical dilemma that is the "right" thing to do, although none of the stakeholders' material interests are benefited. Ethical dilemmas that involve many stakeholders require a reasoning process that clearly states the dilemma objectively, and then proceeds to articulate the issues and different solution alternatives.

Although ethical reasoning has been defined, in part, by acting on "principled thinking," it is also true that moral creativity, negotiating skills, and knowing your own values also help solve tough "real world" situations. Should Louise Simms move to close the lucrative deal or not? Is the official offering her a bribe? What other personal, as well as professional, obligations would she be committing herself to if she accepted? Is the official's request legal? Is it ethical? Is this a setup? If so, who is setting her up? Would Louise be held individually responsible if something went wrong? Who is going to protect her if legal complications arise? How is she supposed to negotiate such a deal? What message is she sending about herself as well as her company? What if she is asked to return and work with these people if the contract is signed? What does Louise stand to win and lose if she does or does not accept the official's offer?

So, what *should* Louise do to act morally responsible in this situation? Is she acting only on behalf of her company or also from her own integrity and beliefs? These are the kinds of questions and issues this chapter raises. No easy answers may exist, but understanding the ethical principles discussed at the outset, sharing ethical dilemmas and outcomes, discussing ethical experiences in depth, and using role plays to analyze situations can help you identify, think, and feel through the issues that underlie ethical dilemmas.

The Louise Simms scenario may be complicated by the international context. This is a good starting point for a chapter on ethics, because business transactions now increasingly involve international players and different "rules of engagement." Chapter 8, on the global environment and stakeholder issues peculiar to multinational corporations, offers additional guidelines for solving dilemmas in international contexts. Deciding what is right and wrong in an international context also involves understanding laws and customs, and the level of economic, social, and technological development of the nation or region involved. For example, do European and U.S. standards of doing business in other countries involve certain biases? Would these biases result in consequences that are beneficial or harmful to those in the local culture? On the other hand, we should not easily accept stereotypical descriptions of how to do business by means of what may be considered "local customs." The remainder of this chapter has additional information and ethical assessments and insights on identifying and resolving the moral dimensions of dilemmas in the workplace and in organizational and personal roles and relationships.

Ethical Insight 2.2

Your Ethical Dilemma

Complete the following steps:

Step 1: Describe an ethical dilemma that you recently experienced. Be detailed: What was the situation? Who did it involve? Why? What happened? What did you do? What did you not do? Describe your reasoning process in taking or not taking action. What did others do to you? What was the result?

Step 2: Read the descriptions of relativism, utilitarianism, universalism, rights, justice, and moral decision making in this chapter. Explain which principle best describes your reasoning and your action(s) in the dilemma you presented in Step 1.

Step 3: Were you conscious that you were reasoning and acting on these (or other) ethical principles before, during, and after your ethical dilemma? Explain.

Step 4: After reading this chapter, would you have acted any differently in your dilemma than you did? Explain.

Moral Creativity

Moral creativity or imagination relates to the need for and skill of recognizing the complexity of some ethical dilemmas that involve interlocking, conflicting interests, and relationships from the point of view of the person, group, and/or organization facing a decision to be made. Creativity is required to gain perspective among the different stakeholders and their interests to sort out and evaluate harmful effects among different alternative actions.[51] What begins as a business-as-usual decision can evolve into a dilemma or even a "defining moment" in one's life.[52] According to Joseph Badaracco at Harvard University,

> An ethical decision typically involves choosing between two options: one we know to be right and another we know to be wrong. A defining moment, however, challenges us in a deeper way by asking us to choose between two or more ideals in which we deeply believe. Such challenges rarely have a "correct" response. Rather, they are situations created by circumstance that ask us to step forward and, in the words of the American philosopher John Dewey, "form, reveal, and test" ourselves. We form our character when we commit to irreversible courses of action that shape our personal and professional identities. We reveal something new about us to ourselves and others because defining moments uncover something that had been hidden or crystallize something that had been only partially known. And we test ourselves because we discover whether we will live up to our personal ideals or only pay them lip service.[53]

Badaracco offers three key questions with creative probes for individuals, work group managers, and company executives to address before acting in a

"defining moment." For individuals, the key question is "Who am I?" This question requires individuals to:

1. Identify their feelings and intuitions that are emphasized in the situation.
2. Identify their deepest values in conflict brought up by the situation.
3. Identify the best course of action to understand the right thing to do.[54]

Work group managers can ask, "Who are we?" They can also address these three dimensions of the team and situation:

1. What strong views and understanding of the situation do others have?
2. Which position or view would most likely win over others?
3. Can I coordinate a process that will reveal the values I care about in this organization?

Company executives can ask, "Who is the company?" Three questions they can consider are:

1. Have I strengthened my position and the organization to the best of my ability?
2. Have I considered my organization's role vis-à-vis society and shareholders boldly and creatively?
3. How can I transform my vision into action, combining creativity, courage, and shrewdness?

CEOs and professionals could ask the three sets of questions to help articulate a morally creative response to ethical dilemmas and "defining moments." What might have happened differently had Bernard Madoff, who executed an unprecedented Ponzi scheme fraud that lasted over decades and defrauded customers of $20 billion, sat down, looked in the mirror, and reflected on these questions? Or what could have happened to Enron's Jeffrey Skilling and Ken Lay, or Tyco's Dennis Kozlowski, or Gary Winnick at Global Crossing?

Ethical Dilemma Problem Solving

A range of decision-making resources can help you evaluate moral possibilities and insights when resolving ethical dilemmas. Change begins with having an awareness that can help build confidence by perceiving dilemmas before they are played out and assists you in negotiating solutions with a moral dimension.

12 Questions to Get Started

A first step in addressing ethical dilemmas is to identify the problem. This is particularly necessary for a stakeholder approach, because the problems depend

on who the stakeholders are and what their stakes entail. Before specific ethical principles are discussed, let's begin by considering important decision criteria for ethical reasoning. How would you apply the criteria to Louise Simms's situation?

Twelve questions, developed by Laura Nash,[55] to ask yourself during the decision-making period are:

1. Have you defined the problem accurately?
2. How would you define the problem if you stood on the other side of the fence?
3. How did the situation occur?
4. To whom and to what do you give your loyalty as a person and as a member of the corporation?
5. What is your intention in making this decision?
6. How does this intention compare with the probable results?
7. Who could your decision injure?
8. Can you discuss the problem with the affected parties before you make your decision?
9. Are you confident that your decision will be valid over a long period?
10. Could you disclose, without qualm, your decision?
11. What is the symbolic potential of your action if understood? If misunderstood?
12. Under what conditions would you allow exceptions?

The above questions can help individuals openly discuss the responsibilities necessary to solve ethical problems. Sharing these questions can facilitate group discussions, build consensus around shared points, serve as an information source, uncover ethical inconsistencies in a company's values, help a CEO see how senior managers think, and increase the nature and range of choices. The discussion process is cathartic.

To return briefly to the opening case, if Louise Simms considered the first question, she might, for example, define the problem she faces from different perspectives (as discussed in Chapter 1). At the *organizational level*, her firm stands to win a sizable contract if she accepts the government official's conditions. Yet her firm's reputation could be jeopardized in the United States if this deal turned out to be a scandal. At the *societal level*, the issues are complicated. In this Middle Eastern country, this type of bargaining might be acceptable. In the United States, however, Louise could have problems with the Foreign Corrupt Practices Act. At the *individual level*, she must decide if her conscience can tolerate the actions and consequences this deal involves. As a woman, she may be at risk because advances were made toward her. Her self-esteem and integrity have also been damaged. She must consider the costs and benefits that she will incur from her company if she decides to accept or reject this assignment. As you can see, these questions can help Louise clarify her goal of making a decision and determine the price she is willing to pay for that decision.

2.6 Individual Ethical Decision-Making Styles

Individual ethical decision-making styles may also be based on what Stanley Krolick defined as (1) individualism, (2) altruism, (3) pragmatism, and (4) idealism.[56] These four styles are summarized here to complement the social responsibility modes, ethical principles, and moral maturity stages discussed above. Caution must be used when considering any of these schemes to avoid stereotyping. These categories are guides—not prescriptions—for further reflection, discussion, and study.

Individualists are driven by natural reason, personal survival, and preservation. The self is the source and justification of all actions and decisions. Individualists believe that "If I don't take care of my own needs, I will never be able to address the concerns of others."[57] The moral authority of individualists is their own reasoning process, based on self-interest. Individualism is related to the principle of naive ethical relativism and to productivism.

Altruists are concerned primarily with other people. Altruists relinquish their own personal security for the good of others. They would, as an extreme, like to ensure the future of the human race. The altruist's moral authority and motivation is to produce the greatest good for the largest number of people. Unlike utilitarians, altruists would not diligently calculate and measure costs and benefits. Providing benefits is their major concern. Altruists justify their actions by upholding the integrity of the community. They enter relationships from a desire to contribute to the common good and to humankind. Altruists are akin to universalists and philanthropists.

Pragmatists are concerned primarily with the situation at hand, not with the self or the other. The pragmatist's bases for moral authority and motivation are the perceived needs of the moment and the potential consequences of a decision in a specific context. The needs of the moment dictate the importance of self-interest, concern for others, rules, and values. Facts and situational information are justifications for the pragmatist's actions. Pragmatists may abandon significant principles and values to produce certain results. They are closest philosophically to utilitarians. Although this style may seem the most objective and appealing, the shifting ethics of pragmatism make this orientation (and the person who espouses it) difficult and unpredictable in a business environment.

Idealists are driven by principles and rules. Reason, relationships, or the desired consequences of an action do not substitute for the idealist's adherence to principles. Duties are absolute. Idealists' moral authority and motivation are commitment to principles and consistency. Values and rules of conduct are the justification that idealists use to explain their actions. Seen as people with high moral standards, idealists can also be rigid and inflexible. Krolick states, "This absolute adherence to principles may blind the idealist to the potential consequences of a decision for oneself, others, or the situation."[58] This style is related to the social responsibility mode of ethical idealism and to the principle of universalism.

Which of the four styles best characterizes your ethical orientation? The orientation of your colleagues? Your supervisor or boss?

Communicating and Negotiating across Ethical Styles

When working or communicating with an ethical style, you also must observe *the other person's ethical style.* According to Krolick, the first step is to "concede that the other person's values and priorities have their own validity in their own terms and try to keep those values in mind to facilitate the process of reaching an agreement."[59] The following guidelines can help when communicating, negotiating, or working with one of the four ethical styles:

- *Individualist:* Point out the benefits to the other person's self-interest.
- *Altruist*: Focus on the benefits for the various constituencies involved.
- *Pragmatist:* Emphasize the facts and potential consequences of an action.
- *Idealist*: Concentrate on the principles or duties at stake.

Learning to recognize and communicate with people who have other ethical styles and being flexible in accommodating their ethical styles, without sacrificing your own, are important skills for working effectively with others.

2.7 Quick Ethical Tests

In addition to knowing the ethical principles, social responsibility modes, and ethical styles presented in this chapter, businesspeople can take short "ethical tests" before making decisions. Many of these rules reflect the principles discussed in this chapter. These "checkpoints," if observed, could change the actions you would automatically take in ethical dilemmas.

The Center for Business Ethics at Bentley University has articulated six simple questions for the "practical philosopher." Before making a decision or acting, ask the following:

1. Is it right?
2. Is it fair?
3. Who gets hurt?
4. Would you be comfortable if the details of your decision were reported on the front page of your local newspaper?
5. What would you tell your child to do?
6. How does it smell? (How does it feel?)

Other quick ethical tests, some of which are classic, include:

- *The Golden Rule:* "Do unto others as you would have them do unto you." This includes not knowingly doing harm to others.
- *The Intuition Ethic:* We know apart from reason what is right. We have a moral sense about what is right and wrong. We should follow our "gut feeling" about what is right.
- *The Means-Ends Ethic:* We may choose unscrupulous but efficient means to reach an end if the ends are really worthwhile and significant. Be sure the ends are not the means.

- *The Test of Common Sense:* "Does the action I am getting ready to take really make sense?" Think before acting.
- *The Test of One's Best Self*: "Is this action or decision I'm getting ready to take compatible with my concept of myself at my best?"
- *The Test of Ventilation*: Do not isolate yourself with your dilemma. Get others' feedback before acting or deciding.
- *The Test of the Purified Idea:* "Am I thinking this action or decision is right just because someone with authority or knowledge says it is right?" You may still be held responsible for taking the action.[60]

Use these principles and guidelines for examining the motivations of stakeholders' strategies, policies, and actions. Why do stakeholders act and talk as they do? What principles drive these actions?

2.8 Concluding Comments

A definition of ethics and business ethics has been offered along with four types of ethical reasoning to provide a basis for making ethical decisions. Individual stakeholders have a wide range of ethical principles, orientations, and "quick tests" to draw on before solving an ethical dilemma. Moral maturity also affects an individual's ethical reasoning and actions. Kohlberg's stages of moral development and Covey's Moral Continuum are concepts that provide a diagnostic and suggested developmental insights into ethical decision making.

Using moral reflection and creativity is also important when deciding between two "right" or "wrong" choices. Reflecting on one's core values combined with a sense of moral courage and shrewdness are also a recommended part of this decision-making process. When there are multiple stakeholders in a dilemma, the moral dimension of the stakeholder approach can be helpful by identifying the "ground rules" or "implicit morality" of institutional members. As R. Edward Freeman and Daniel Gilbert Jr. state:

> Think of the implicit morality of an institution as the rules that must be followed if the institution is to be a good one. The rules are often implicit, because the explicit rules of an institution may be the reason that the institution functions badly. Another way to think of the implicit morality of an institution is as the internal logic of the institution. Once this internal logic is clearly understood, we can evaluate its required behaviors against external standards.[61]

Back to Louise Simms . . .

Let's return to the opening case in which Louise Simms is trying to decide what to do. Put yourself in Louise's situation. Identify your ethical decision-making style. Are you primarily an idealist, pragmatist, altruist, or individualist? What are some of your blind spots? Consider the three questions regarding a "defining moment" at the beginning of the chapter: Who am I?

Who are we? Who is the company? What courses of action are available after reviewing your responses to these questions? Then, describe the ethical principles you usually follow in your life: utilitarianism, rights, justice, universalism, ethical virtue, ethical relativism, and the common good ethic. Which of those principles do you aspire to use to act more ethically and morally mature and responsible? What is your moral responsibility to yourself, your family and friends, your colleagues and work team, and to the company? How will you feel about yourself after you make the decision? Now make Louise's decision and share your decision with your classmates and consider their responses. Do you think you made the right decision?

Chapter Summary

Complex ethical dilemmas in business situations involve making tough choices between conflicting interests. This chapter began with classic ethical principles that are used to guide dilemmas and decisions at the individual, group, and organizational levels. Moral maturity and the Covey's Moral Continuum were discussed to consider how to approach personal level dilemmas. Questions were presented for addressing dilemmas and "defining moments" creatively, boldly, and shrewdly, as well as 12 questions and three decision criteria that can assist individuals in determining the most suitable course of action.

Individuals can gain a clear perspective of their own motivations and actions by distinguishing them from those of others. This perspective can be useful for guiding your own decision-making process. Understanding the criteria in this chapter can enable you to reason more critically when examining other stakeholders' ethical reasoning.

A primary goal of ethical reasoning is to help individuals act in morally responsible ways. Ignorance and bias are two conditions that cloud moral awareness. Five principles of ethical reasoning were presented to expose you to methods of ethical decision making. Each principle was discussed in terms of the utility and drawbacks characteristic of it. Guidelines for thinking through and applying each principle in a stakeholder analysis were also provided. These principles are not mechanical recipes for selecting a course of action. They are filters or screens to use for clarifying dilemmas.

Three ethical orientations— immoral, amoral, and moral—can be used to evaluate ethics. Immoral and moral motives are more discernible than amoral ones. Amoral orientations include lack of concern for others' interests and well-being. Although no intentional harm or motive may be observed, harmful consequences from ignorance or neglect reflect amoral styles of operating.

Four social responsibility roles or business modes were discussed: productivism and philanthropy (influenced by stockholder concerns) and progressivism and ethical idealism (driven by stockholder concerns but also influenced by external stakeholders). Individuals also have ethical decision-making styles. Four different (but not exclusive) styles are individualism, altruism, pragmatism, and idealism. Another person's ethical decision-making style must be understood when engaging in communication and negotiation. These styles are a starting point for identifying predominant decision-making characteristics.

The final section of this chapter offered quick "ethical tests" that can be used to provide insight into your decision-making process and actions.

Questions

1. Do you believe ethical dilemmas can be prevented and solved morally without the use of principles? Explain. Offer an example from a dilemma you recently experienced or currently are experiencing. Characterize the logic you used in thinking through or having made a decision. Compare the logic you used to principles and quick tests in this chapter. What similarities and differences did you discover? Can you include any of the principles and ethical reasoning in this chapter in dilemmas you may or expect to face? Explain.
2. Why are creativity and moral imagination oftentimes necessary in preventing and resolving ethical dilemmas and "defining moments" of conflict in one's workplace? Offer an example of an ethically questionable situation in which you had to creatively improvise to "do the right thing."
3. What is a first step for addressing ethical dilemmas? What parts of this chapter would and could you use to complement or change your own decision-making methods?
4. How can the discussion on personal level ethical decision making considering moral maturity and the moral continuum assist you in addressing dilemmas in your life and work?
5. What single question is the most powerful for solving ethical dilemmas?
6. What are two conditions that eliminate a person's moral responsibility?
7. Return to the case you selected in question 4 above. Briefly explain which of the chapter's five fundamental principles of ethical reasoning the leaders and/or major stakeholders you identified used and did not use in the case. Which ethical principle(s) would you recommend that they should have used? Why?
8. What are some of the problems characteristic of cultural relativism? Offer an example in the news of a company that has acted unethically according to the perspective of cultural relativism.
9. Why is utilitarianism useful for conducting a stakeholder analysis? What are some of the problems with using this principle? Give an example of when you used utilitarianism to justify an ethically questionable action.
10. Briefly explain the categorical imperative. What does it force you, as a decision maker, to do when choosing an action in a moral dilemma?
11. Explain the difference between the principles of rights and justice. What are some of the strengths and weaknesses of each principle?
12. Which of the four social responsibility modes most accurately characterizes your college/university and place of work? Explain. Do your ethics and moral values agree with these organizations? Explain.
13. Briefly explain your ethical decision-making style as presented in the chapter.
14. How would you describe your level of moral maturity using Kohlberg's stages?

15. What insights did you gain from Covey's Moral Continuum with regard to your ethical decision-making activities? What are some connections between Covey's and Kohlberg's concepts and ethics?
16. Explain what ethical logic and actions people generally take to persuade you to do something that is ethically questionable. Refer to the ethical decision styles in the chapter.
17. Which of the ethical "quick tests" do you prefer? Why?

Exercises

1. Describe a serious ethical dilemma you have experienced. Use the 12 questions developed by Laura Nash to offer a resolution to the problem, even if your resolution is different from the original experience. Did you initially use any of the questions? Would any of these questions have helped you? How? What would you have done differently? Why?
2. Identify an instance when you thought ignorance absolved a person or group from moral responsibility. Then identify an example of a person or group failing to become fully informed about a moral situation. Under what conditions do you think individuals are morally responsible for their actions? Why?
3. With which of the four social responsibility business modes in the chapter do you most identify? Why? Name a company that reflects this orientation. Would you want to work for this company? Would you want to be part of the management team? Explain.
4. Select a corporate leader in the news who acted legally but immorally and one who acted illegally but morally. Explain the differences of the actions and behaviors in each of the two examples. What lessons do you take from your examples?
5. Select two organizations in the same industry that you are familiar with or that are in the media or online news, such as McDonald's and Burger King, Toyota and General Motors, Virgin Airlines and American Airlines. Research some of the latest news items and activities about each company and its officers over the same time period. Now, using ethical principles and quick tests from this chapter, compare and contrast each. Evaluate how "ethical" each is compared to the other.

Real-Time Ethical Dilemma

I was employed as a certified public accountant (CPA) for a regional accounting firm that specialized in audits of financial institutions and had many local clients. My responsibilities included supervising staff, collecting evidence to support financial statement assertions, and compiling work papers for managers and partners to review. During the audit of a publicly traded bank, I discovered that senior bank executives were under investigation by the Federal Deposit Insurance Corporation (FDIC) for removing funds from the bank. They were also believed to be using bank funds to pay corporate credit card bills for gas and spouses' expenses. The last allegation noted that the executives were issuing loans to relatives without proper collateral.

After reviewing the work papers, I found two checks made payable to one executive of the bank that were selected during a cash count from two tellers. There was no indication based on our sampling that expenses were being paid for spouses. My audit manager and the chief financial officer (CFO) of my firm were aware of these problems.

After the fieldwork for the audit was completed, I was called into the CEO's office. The CEO and the chief operating officer (COO) stated that the FDIC examiners wanted to interview the audit manager, two staff accountants, and me. The CEO then asked the following question: "If you were asked by the FDIC about a check or checks made payable to bank executives, how would you answer?" I told them that I would answer the FDIC examiners by stating that, during our audit, we made copies of two checks made payable to an executive of the bank for $8,000 each.

The COO stated that during his review of the audit work papers he had not found any copies of checks made payable to executives. He also stated that a better response to the question regarding the checks would be, "I was not aware of reviewing any checks specifically made payable to the executive in question." The COO then said that the examiners would be in the following day to speak with the audit staff. I was dismissed from the meeting.

Neither the CEO nor the COO asked me if the suggested "better" response was the response I would give, and I did not volunteer the information. During the interview, the FDIC investigators never asked me whether I knew about the checks. Should I have volunteered this information?

Questions

1. What would you have done? Volunteered the information or stayed silent? Explain your decision.
2. Was anything unethical going on in this case? Explain.
3. Describe the "ethics" of the officers of the firm in this case.
4. What, if anything, should the officers have done, and why?
5. What lessons, if any, can you take from this case, as an employee working under company officials who have more power than you do?

Cases

Case 3

Ford's Pinto Fires: The Retrospective View of Ford's Field Recall Coordinator

Brief Overview of the Ford Pinto Fires

Determined to compete with fuel-efficient Volkswagen and Japanese imports, the Ford Motor Company introduced the subcompact Pinto in the 1971 model year. Lee Iacocca, Ford's president at the time, insisted that the Pinto weigh no more than 2,000 pounds and cost no more than $2,000. Even with these restrictions, the Pinto met federal safety standards, although some people have argued that strict adherence to the restrictions led Ford engineers to compromise safety. Some 2 million units were sold during the 10-year life of the Pinto.

The Pinto's major design flaw—a fuel tank prone to rupturing with moderate-speed rear-end collisions—surfaced not too long after the Pinto's entrance to the market. In April 1974, the Center for Auto Safety petitioned the National Highway Traffic Safety Administration (NHTSA) to recall Ford Pintos due to the fuel tank design defect. The Center for Auto Safety's petition was based on reports from attorneys of three deaths and four serious injuries in moderate-speed rear-end collisions involving Pintos. The NHTSA did not act on this petition until 1977.

As a result of tests performed for the NHTSA, as well as the extraordinary amount of publicity generated by the problem, Ford agreed, on June 9, 1978, to recall 1.5 million 1971–1976 Ford Pintos and 30,000 1975–1976 Mercury Bobcat sedan and hatchback models for modifications to the fuel tank. Recall notices were mailed to the affected Pinto and Bobcat owners in September 1978. Repair parts were to be delivered to all dealers by September 15, 1978.

Unfortunately, the recall was initiated too late for six people. Between June 9 and September 15, 1978, six people died in Pinto fires after a rear impact. Three of these people were teenage girls killed in Indiana in August 1978 when their 1973 Pinto burst into flames after being rear-ended by a van. The fiery deaths of the Indiana teenagers led to criminal prosecution of the Ford Motor Company on charges of reckless homicide, marking the first time that an American corporation was prosecuted on criminal charges. In the trial, which commenced on January 15, 1980, "Indiana state prosecutors alleged that Ford knew Pinto gasoline tanks were prone to catch fire during rear-end collisions but failed to warn the public or fix the problem out of concern for profits." On March 13, 1980, a jury found Ford innocent of the charges. Production of the Pinto was discontinued in the fall of 1980.

Enter Ford's Field Recall Coordinator

Dennis A. Gioia, currently a professor in the Department of Management and Organization at Pennsylvania State University, was the field recall coordinator at Ford Motor Company as the Pinto fuel tank defect began unfolding. Gioia's responsibilities included the operational coordination of all the current recall

campaigns, tracking incoming information to identify developing problems, and reviewing field reports of alleged component failures that led to accidents. Gioia left Ford in 1975. Subsequently, "reports of Pinto fires escalated, attracting increasing media attention." The remainder of this case, written in Gioia's own words in the early 1990s, is his personal reflection on lessons learned from his experiences involving the Pinto fuel tank problem.

Why Revisit Decisions from the Early 1970s?

I take this case very personally, even though my name seldom comes up in its many recountings. I was one of those "faceless bureaucrats" who is often portrayed as making decisions without accountability and then walking away from them—even decisions with life-and-death implications. That characterization is, of course, far too stark and superficial. I certainly don't consider myself faceless, and I have always chafed at the label of bureaucrat as applied to me, even though I have found myself unfairly applying it to others. Furthermore, I have been unable to walk away from my decisions in this case. They have a tendency to haunt—especially when they have had such public airings as those involved in the Pinto fires debacle have had.

But why revisit 20-year-old decisions, and why take them so personally? Here's why: because I was in a position to do something about a serious problem . . . and didn't. That simple observation gives me pause for personal reflection and also makes me think about the many difficulties people face in trying to be ethical decision makers in organizations. It also helps me to keep in mind the features of modern business and organizational life that would influence someone like me (me of all people, who purposely set out to be an ethical decision maker!) to overlook basic moral issues in arriving at decisions that, when viewed retrospectively, look absurdly easy to make. But they are not easy to make, and that is perhaps the most important lesson of all.

The Personal Aspect

I would like to reflect on my own experience mainly to emphasize the personal dimensions involved in ethical decision making. Although I recognize that there are strong organizational influences at work as well, I would like to keep the critical lens focused for a moment on me (and you) as individuals. I believe that there are insights and lessons from my experience that can help you think about your own likely involvement in issues with ethical overtones.

First, however, a little personal background. In the late 1960s and early 1970s, I was an engineering/MBA student; I also was an "activist," engaged in protests of social injustice and the social irresponsibility of business, among other things. I held some pretty strong values, and I thought they would stand up to virtually any challenge and enable me to "do the right thing" when I took a career job. I suspect that most of you feel that you also have developed a strongly held value system that will enable you to resist organizational inducements to do something unethical. Perhaps. Unfortunately, the challenges do not often come in overt forms that shout the need for resistance or ethical righteousness. They are much

more subtle than that, and thus doubly difficult to deal with because they do not make it easy to see that a situation you are confronting might actually involve an ethical dilemma.

After school, I got the job of my dreams with Ford and, predictably enough, ended up on the fast track to promotion. That fast track enabled me to progress quickly into positions of some notable responsibility. Within two years I became Ford's field recall coordinator, with first-level responsibility for tracking field safety problems. It was the most intense, information-overloaded job you can imagine, frequently dealing with some of the most serious problems in the company. Disasters were a phone call away, and action was the hallmark of the office where I worked. We all knew we were engaged in serious business, and we all took the job seriously. There were no irresponsible bureaucratic ogres there, contrary to popular portrayal.

In this context, I first encountered the neophyte Pinto fires problem—in the form of infrequent reports of cars erupting into horrendous fireballs in very low-speed crashes and the shuddering personal experience of inspecting a car that had burned, killing its trapped occupants. Over the space of a year, I had two distinct opportunities to initiate recall activities concerning the fuel tank problems, but on both occasions, I voted not to recall, despite my activist history and advocacy of business social responsibility.

The key question is how, after two short years, could I have engaged in a decision process that appeared to violate my own strong values—a decision process whose subsequent manifestations continue to be cited by many observers as a supposedly definitive study of corporate unethical behavior? I tend to discount the obvious accusations: that my values weren't really strongly held; that I had turned my back on my values in the interest of loyalty to Ford; that I was somehow intimidated into making decisions in the best interest of the company; that despite my principled statements, I had not actually achieved a high stage of moral development; and so on. Instead, I believe a more plausible explanation for my own actions looks to the foibles of normal human information processing.

I would argue that the complexity and intensity of the recall coordinator's job required that I develop cognitive strategies for simplifying the overwhelming amount of information I had to deal with. The best way to do that is to structure the information into cognitive "schemas," or more specifically "script schemas," that guide understanding and action when facing common or repetitive situations. Scripts offer marvelous cognitive shortcuts because they allow you to act virtually unconsciously and automatically, and thus permit you to handle complicated situations without being paralyzed by needing to think consciously about every little thing. Such scripts enabled me to discern the characteristic hallmarks of problem cases likely to result in recall and to execute a complicated series of steps required to initiate a recall.

All of us structure information all of the time; we could hardly get through the workday without doing so. But there is a penalty to be paid for this wonderful cognitive efficiency: we do not give sufficient attention to important information that requires special treatment because the general information pattern has

surface appearances that indicate that automatic processing will suffice. That, I think, is what happened to me. The beginning stages of the Pinto case looked for all the world like a normal sort of problem. Lurking beneath the cognitive veneer, however, was a nasty set of circumstances waiting to conspire into a dangerous situation. Despite the awful nature of the accidents, the Pinto problem did not fit an existing script; the accidents were relatively rare by recall standards, and the accidents were not initially traceable to a specific component failure. Even when a failure mode suggesting a design flaw was identified, the cars did not perform significantly worse in crash tests than competitor vehicles. One might easily argue that I should have been jolted out of my script by the unusual nature of the accidents (very low speed, otherwise unharmed passengers trapped in a horrific fire), but those facts did not penetrate a script cued for other features. (It also is difficult to convey to the lay person that bad accidents are not a particularly unusual feature of the recall coordinator's information field. Accident severity is not necessarily a recall cue; frequently repeated patterns and identifiable causes are.)

The Corporate Milieu

In addition to the personalized scripting of information processing, there is another important influence on the decisions that led to the Pinto fires mess: the fact that decisions are made by individuals working within a corporate context. It has escaped almost no one's notice that the decisions made by corporate employees tend to be in the best interest of the corporation, even by people who mean to do better. Why? Because the socialization process and the overriding influence of organizational culture provide a strong, if generally subtle, context for defining appropriate ways of seeing and understanding. Because organizational culture can be viewed as a collection of scripts, scripted information processing relates even to organizational-level considerations. Scripts are context bound; they are not free-floating general cognitive structures that apply universally. They are tailored to specific contexts. And there are few more potent contexts than organizational settings.

There is no question that my perspective changed after joining Ford. In retrospect, I would be very surprised if it hadn't. In my former incarnation as a social activist, I had internalized values for doing what was right–as I understood righteousness in grand terms, but I had not internalized a script for applying my values in a pragmatic business context. Ford and the recall coordinator role provided a powerful context for developing scripts–scripts that were inevitably and undeniably oriented toward ways of making sense that were influenced by the corporate and industry culture.

I wanted to do a good job, and I wanted to do what was right. Those are not mutually exclusive desires, but the corporate context affects their synthesis. I came to accept the idea that it was not feasible to fix everything that someone might construe as a problem. I therefore shifted to a value of wanting to do the greatest good for the greatest number (an ethical value tempered by the practical constraints of an economic enterprise). Doing the greatest good for the

greatest number meant working with intensity and responsibility on those problems that would spare the most people from injury. It also meant developing scripts that responded to typical problems, not odd patterns like those presented by the Pinto.

Another way of noting how the organizational context so strongly affects individuals is to recognize that one's personal identity becomes heavily influenced by corporate identity. As a student, my identity centered on being a "good person" (with a certain dose of moral righteousness associated with it). As recall coordinator, my identity shifted to a more corporate definition. This is an extraordinarily important point, especially for students who have not yet held a permanent job role, and I would like to emphasize it. Before assuming your career role, identity derives mainly from social relationships. Upon putting on the mantle of a profession or a responsible position, identity begins to align with your role. And information processing perspective follows from the identity.

I remember accepting the portrayal of the auto industry and Ford as "under attack" from many quarters (oil crises, burgeoning government regulation, inflation, litigious customers, etc.). As we know, groups under assault develop into more cohesive communities that emphasize commonalities and shared identities. I was by then an insider in the industry and the company, sharing some of their beleaguered perceptions that there were significant forces arrayed against us and that the well-being of the company might be threatened.

What happened to the original perception that Ford was a socially irresponsible giant that needed a comeuppance? Well, it looks different from the inside. Over time, a responsible value for action against corporate dominance became tempered by another reasonable value that corporations serve social needs and are not automatically the villains of society. I saw a need for balance among multiple values, and as a result, my identity shifted in degrees toward a more corporate identity.

The Torch Passes to You

So, given my experiences, what would I recommend to you, as a budding organizational decision maker? I have some strong opinions. First, develop your ethical base now! Too many people do not give serious attention to assessing and articulating their own values. People simply do not know what they stand for because they haven't thought about it seriously. Even the ethical scenarios presented in classes or executive programs are treated as interesting little games without apparent implications for deciding how you intend to think or act. These exercises should be used to develop a principled, personal code that you will try to live by. Consciously decide your values. If you don't decide your values now, you are easy prey for others who will gladly decide them for you or influence you implicitly to accept theirs.

Second, recognize that everyone, including you, is an unwitting victim of his or her cognitive structuring. Many people are surprised and fascinated to learn that they use schemas and scripts to understand and act in the organizational world. The idea that we automatically process so much information so much of

the time intrigues us. Indeed, we would all turn into blithering idiots if we did not structure information and expectations, but that very structuring hides information that might be important–information that could require you to confront your values. We get lulled into thinking that automatic information processing is great stuff that obviates the necessity for trying to resolve so many frustrating decisional dilemmas.

Actually, I think too much ethical training focuses on supplying standards for contemplating dilemmas. The far greater problem, as I see it, is recognizing that a dilemma exists in the first place. The insidious problem of people not being aware that they are dealing with a situation that might have ethical overtones is another consequence of schema usage. I would venture that scripted routines seldom include ethical dimensions. Is a person behaving unethically if the situation is not even construed as having ethical implications? People are not necessarily stupid, ill-intentioned, or Machiavellian, but they are often unaware. They do indeed spend much of their time cruising on automatic, but the true hallmark of human information processing is the ability to switch from automatic to controlled information processing. What we really need to do is to encourage people to recognize cues that build a "Now Think!" step into their scripts–waving red flags at yourself, so to speak–even though you are engaged in essentially automatic cognition and action.

Third, because scripts are context bound and organizations are potent contexts, be aware of how strongly, yet how subtly, your job role and your organizational culture affect the ways you interpret and make sense of information (and thus affect the ways you develop the scripts that will guide you in unguarded moments). Organizational culture has a much greater effect on individual cognition than you would ever suspect.

Last, be prepared to face critical responsibility at a relatively young age, as I did. You need to know what your values are and you need to know how you think so that you can know how to make a good decision. Before you can do that, you need to articulate and affirm your values now, before you enter the fray. I wasn't really ready. Are you?

Questions for Discussion

1. The Ford Pinto met federal safety standards, yet it had a design flaw that resulted in serious injuries and deaths. Is simply meeting safety standards a sufficient product design goal of ethical companies?
2. Gioia uses the notion of script schemas to help explain why he voted to not initiate a recall of the Ford Pinto. In your opinion, is this a justifiable explanation?
3. How can organizational context influence the decisions made by organizational members?
4. If you had been in Gioia's position, what would you have done? Why?
5. Describe the four key decision-making lessons that Gioia identifies for neophyte decision makers. Discuss how you expect or intend to use these four lessons in your own career.

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Case 4

Jerome Kerviel: Rogue Trader or Misguided Employee? What Really Happened at the Société Générale?

Société Générale: A French Bank Globally Recognized

The French banking company Société Générale ("SocGen" or "the Company") was founded on May 4, 1864, and at the time of writing is headed by co-CEOs Philippe Citerne and Daniel Bouton. The bank has grown to serve 19.2 million individual customers in 76 countries. It employs 103,000 workers from 114 different nationalities. SocGen operates in three major businesses: retail banking and financial services, global investment management and services, and corporate and investment banking. The core values at the Company are professionalism, team spirit, and innovation.

In 2006, SocGen ranked 67 on *Fortune*'s 2006 Global 500 and had managed to build a $72 billion position in European stock index futures. The year before, the Company ranked 152 on *Fortune*'s list. In addition to top-line growth, SocGen also posted a more important improvement in overall profitability, at $5.5 billion, up 42% from the prior year. It was the 14th largest company among the banking institutions on the list.

The Beginning of the Story

Things were about to change for SocGen. Recent turmoil in 2006 revolved around the collapsing housing market and a mortgage industry that witnessed loan defaults in record numbers. Several banks engaged in purchasing high-risk mortgage loans, but the overall economic recession, primarily in the United States but also felt globally, constrained this bank's financial status. SocGen saw its stock price cut almost in half throughout the year, but this was not the only potential pitfall for this once robust Company. It was the actions of one rogue trader, Jerome Kerviel, that could have brought about the ultimate downfall of SocGen.

Who Is Jerome Kerviel and What Happened at the Bank?

On January 24, 2008, Jerome Kerviel found himself in the international media spotlight, but not as he would have hoped. On this day, SocGen announced to the world that it had discovered a $7.14 billion trading fraud caused by a single trader, Kerviel. Additionally, a nearly $3 billion loss was posted due to the loss in investments in the U.S. subprime mortgage industry. The second largest bank in France had its shares halted to avoid a complete market collapse on the price of the stock.

From his modest roots to the upscale Paris suburb where he resided, friends and family never expected that this unmarried 31 year old could be capable of such a scandal. With a relatively modest salary ($145,700), Kerviel did not profit from his trading scheme. He had been an employee at SocGen since 2000. He began in a monitoring support role, and oversaw the futures traders for five years.

He was then promoted to the futures trading desk. He traded European futures by betting on the future performance of these funds. Kerviel saw his trading profits increase throughout 2007 as he bet that the markets would fall during this time. By the end of the year, he needed to mask his significant gains, so he created fictional losing positions to erode his gains. These included the purchasing of 140,000 DAX futures (the German stock index: a blue chip stock market index that includes the 30 major German companies trading on the Frankfurt Stock Exchange). By mid-January, Kerviel had lost over $3 billion. He was hedging more than $73.3 billion, an amount far in excess of the trading limits created by SocGen for a single trader. This amount even exceeded SocGen's overall market cap of $52.6 billion.

Despite five levels of increased security to prevent traders from assuming positions greater than a predetermined amount, and a group compliance division in charge of monitoring trader activity, Kerviel was able to bypass internal controls for over two years.

Kerviel's motive was not to steal from the bank, but to have his significant trading gains catapult his career, and to cash in on a significant bonus given to traders who exhibit the type of profitability he created for the Company. Red flags were triggered, but e-mails to his superiors on his trading activity were ignored due to his overall profitability for the Company. Kerviel admitted his wrongdoing, but stated that SocGen was partially responsible for not monitoring his activities correctly and by having rewarded his behavior with a proposed bonus of $440,000. Kerviel stated that his actions were similar to those of other traders; he was just being labeled as the scapegoat in this investigation.

Company Reaction

Once the fraud was detected in mid-January 2008, SocGen immediately reported it to France's central bank, Bank of France. Over the next three trading days, SocGen employees began to unload all of Kerviel's positions into the marketplace. The Company attempted to complete this significant sale of securities in a manner that would not disrupt the normal market movement. The ripple effect of this action may have created additional pressure on the already falling world markets. Some analysts speculated that this action may even have influenced the U.S. Federal Reserve rate cut. SocGen management denied that action after it discovered that the trading fraud had a meaningful impact on the world marketplace. Co-CEO Bouton stated that the three-day sell-off was in accordance with guidelines, and that the liquidation of a position at any one time could not be more than 10% of the given market.

After Kerviel admitted his guilt, his employment was terminated along with that of his supervisors. Bouton submitted a formal resignation, along with second-in-command Phillipe Citerne; however, both were rejected by the board of directors. Employees at the Company staged demonstrations where they showed their support for Bouton.

The bank has stated that since the activity was brought to light, there has been a tightening on the internal controls, so that actions such as Kerviel's are

no longer possible for a trader. On January 25, 2008, SocGen took out a full-page newspaper article apologizing to its customers for the scandal. On January 30, the board announced the formation of an independent committee to investigate the current monitoring practices and determine what measures could be put in place to prevent it from happening again. The committee would enlist the services of the auditing company PricewaterhouseCoopers. The Company also announced that it needed an influx of capital to stay afloat, and began looking to outside help to raise $8.02 billion in new capital.

Government Reaction

On January 26, 2008, Kerviel was taken into police custody for questioning regarding his trading activity at SocGen. Three complaints were issued to police, one by SocGen and two others by small shareholders.

This event was the focus at the World Economic Forum in Davos, Switzerland, which brought to light questions on how risk is managed within organizations. French finance minister Christine Lagarde was assigned the task of investigating the events and compiling a report on the failure of internal controls at SocGen. The report was then publicized in an effort to prevent similar fraudulent trading events from occurring in the future. A timeline of the events leading up to the trading losses was created in an effort to better understand the events that transpired. In the report, Lagarde stated that there should be an increase in penalties for banks that violate the commission's set rules. The then president of France, Nicolas Sarkozy, stated that the events at SocGen did not affect the "solidity and reliability of France's financial system." He wanted the board of directors to take action against senior management, including Bouton.

On January 28, 2008, Kerviel was charged with unauthorized computer activity and breach of trust. Plans to charge Kerviel with fraud and misrepresentation were also announced, which could carry a maximum prison time of seven years and fines of $1.1 million. At the time of writing, the fraud charge had not been accepted by the courts; however, prosecutors were seeking to appeal this to a higher court.

The government sought to prevent a hostile takeover of SocGen during this period. However, the European Union was in disagreement with the French government and stated that all bidders should be treated equally: "The same rules apply as in other takeover situations under free movement of capital rules. Potential bidders are to be treated in an undiscriminatory manner." The current standout bidder is the largest bank in France, BNP Paribas. Many competitors are contemplating making an offer for the distressed Company—to purchase a portion or all of the bank's assets.

Why It Happened

Kerviel was able to evade detection because of his experience monitoring the traders in his early years at SocGen. Falsifying bank records and computer fraud were part of the intricate scheme that he created. Kerviel knew when he would be monitored by the bank and avoided any activity during those periods.

He created a fictitious company and falsified trading records to keep his activity under wraps. Kerviel also used other employees' computer access codes and falsified trading documents.

Related Companies with Similar Troubles

In 1995, Barings, a British bank that had been in existence for more than 230 years, collapsed as the results of the actions of one futures trader, Nick Leeson. Leeson lost more than $1.38 billion when trading futures in the Asian markets.

In 1991, London-based Bank of Credit and Commerce International (BCCI) went bankrupt as the result of illegal trading activity and insider trading, losing over $10 billion.

During the late 1980s and early 1990s, Yasuo Hamanaka, a Japanese copper futures trader, cost his employer, Sumitomo Copper, $2.6 billion.

Is There More to the Story?

A director of SocGen, Robert Day, sold $126.1 million in shares on January 9, 2008, two weeks before the trading fraud was disclosed. He also sold $14.1 million the next day for two charitable trusts he chaired. Trading also occurred on January 18. The total trading activity amounted to $206 million. It was reported that Day traded during the timeframe where it was acceptable for a board member to trade shares of stock. Accusations of insider trading have been denied.

The *Financial Times* in London has reported that SocGen may have known about the trading activities back in November, when the Eurex derivatives exchange questioned Kerviel's trading positions and alerted the Company. This then calls into question the lack of oversight by the Company, and what responsibility SocGen has to its shareholders for this oversight. Kerviel accuses his supervisors of turning a blind eye to his activities because he was earning the Company a significant amount of money. He states that his profits should have raised concerns because they far exceeded the parameters of the transactions he was allowed to engage in.

Corporate Controls at SocGen

It has been stated that there were not enough safeguards in place to protect the bank from Kerviel's activities. The following describes the existing safeguards and focuses on the public ethical programs that SocGen had in place.

At SocGen, the board of directors and three corporate governance committees that were established in 1995 are in charge of creating and policing the Company through its internal rules and regulations. The Company engages in risk management by constantly reviewing its risk exposure in the variety of areas in which it operates. Due to the sensitivity of many of its banking projects, corporate governance remains at the forefront of the bank's activities. The three committees include the audit committee (in charge of review of the Company's draft financial statements prior to submission to the board of directors), the compensation committee (in charge of determining executive compensation packages),

and the nomination committee (appoints new board members and executive officers).

The board of directors is responsible for the Company's overall strategy and the adherence to its defined set of internal rules. The risk assessment divisions operate autonomously from the other operating units. Reporting directly to general management, this group consists of 2,000 employees who constantly monitor the activities of the other business units, making sure they are in compliance with the internal rules established by the board of directors. Monthly meetings are held to review strategic initiatives and all new products must first receive the approval of the risk team before implementation may take place.

Internal audit groups have been put in place with the following assignments:

- Detect, measure, and manage the risks incurred.
- Guarantee the reliability, integrity, and availability of financial and management data.
- Verify the quality of the information and communications systems.

All staff members are under constant day-to-day supervision to ensure their compliance with the regulations in place.

The Compliance Department was established in 1997 and is currently responsible for monitoring all banking activities so that the actions of all employees are in the best interest of the Company. A charter is in place that extends beyond local law and attempts to cover the high ethical standards set by the Company. Three key principles of the group are to work only with well-known customers, always assess the economic legitimacy of the action, and have the ability to justify any stance taken.

The trading room had eight compliance staff members in 2006, with the goal of increasing this number in 2007. Anti-money laundering practices have also been in the spotlight during the last few years. In all, the group has increased overall training for 2006 to 50,000 hours, up from 24,000 in 2005. The total number of employees trained is 18,000 individuals.

The role of information technology (IT) has also increased in order to support the corporate governance initiative. GILT (Group Insider List Tool) monitors potential conflicts of interest and insider-trading activity within the Company, and MUST (Monitoring of Unusual and Suspicious Transactions) is used to detect insider trading and market manipulation. The Company also has standards in place to prevent corruption on the part of Company employees and government officials.

A Code of Conduct has been in place since March 2005, with the goal of being a reference tool for employees that highlights the principles that the Company wants its employees to uphold. The Code was created as the result of the changes in the current business environment, since employees and society alike have set a higher standard for an individual Company's corporate responsibilities. Like many other companies that have a Code of Conduct, SocGen felt that

establishing this Code was an essential part of operating in the current business environment.

The SocGen China Group has established strict controls in an effort to prevent internal private information and confidential customer data from leaking to the outside marketplace. Separation is a key component in this, whereby an effort is made to eliminate the chance of conflicts of interest on sensitive projects. There is restricted access to IT programs, and any potential conflict of interest must first be approved and signed off by the Compliance Department.

Compliance structures were put in place beginning in March 2005 as a result of a change in law by the French Banking and Financial Regulation Committee (Regulation No. 97–02). The secretary-general of SocGen heads the Group Compliance Committee. Through monthly meetings, members of the group identify any potential risks on the part of the Company, develop ways to prevent future risks in new products, and engage in employee training in an effort to strengthen the idea of corporate compliance within the company culture.

Stakeholders and Their Roles

The main stakeholder in this case is Jerome Kerviel. His actions were the primary driver behind the significant losses incurred by SocGen. However, although Kerviel may have been the focal stakeholder, there are several other primary stakeholders. Kerviel's direct supervisors were responsible for managing his actions. Senior management and the board of directors were responsible for implementing and enforcing guidelines. Employees of the Company are stakeholders since other traders' actions may have influenced Kerviel's decisions, and the Kerviel case may have jeopardized their own careers within the Company. The final primary stakeholders were the Company's shareholders, who were negatively impacted by the huge trading losses at SocGen brought about by Kerviel.

Secondary stakeholders include the government, who pushed the board of directors for Bouton's resignation, and the court systems prosecuting Kerviel and other individuals indicted on counts of insider trading. There are competitors, including BNP Paribas, who may try to take advantage of this opportunity to purchase a portion of SocGen's operations at a devalued price. Finally, there is the public at large, whose confidence was yet again shaken by another scandal within a financial institution.

Potential coalitions involved in the events leading up to the trading scandal include traders and their managers who may have ignored rules and regulations enacted by the governing committee at SocGen. Current coalitions may include shareholders who want to be reimbursed for the management oversight. Shareholder suits may also be brought against those identified as potentially engaging in insider trading. Finally, competition may be forming a coalition to section off the different business units of SocGen to complete a proposed buyout offer.

From the CEO's perspective, Kerviel might be seen as directly violating the rules put in place by the governing committee. Kerviel's managers also did not fully adhere to the established policies. The board of directors and the CEO

were instrumental in the creation of the guidelines. The board rejected Bouton's letter of resignation and many employees have been very supportive of him, stating that he was the person who could guide the Company through this trying time.

Each stakeholder in this case had varying degrees of power. Kerviel had the power to operate with limited supervision (although this was due to his manipulation of the system) and to have a significant impact on the overall bottom line at SocGen. The supervisors of the traders had a degree of power only over the traders, provided they were not blindsided by the traders' fraudulent activities. The board of directors was responsible for providing strategic guidance for the Company, electing a CEO, and establishing rules and regulations for the Company and its employees. The shareholders of SocGen stock had the power to vote on issues, since they are each individual owners of the Company. The government had the power to influence how companies conducted business. The competitors impact the strategies a Company must undertake in order to stay ahead of its competition.

Three Primary Stakeholders and Their Obligations

Kerviel had a legal obligation not to engage in fraudulent behavior; this is evidenced by the fact that he was indicted in the French court system. His economic incentive was to make the most money possible for SocGen while minimizing risk. He was successful for two years, but as he failed to minimize overall risk, his behavior eventually caught up with him. He had an ethical responsibility to management and his colleagues. He could be viewed as both a threat to the Company and a cooperative influence, depending on how management controlled the situation.

Kerviel's supervisors did not have as significant a legal obligation as Kerviel with regard to his specific responsibilities and actions. However, if they had been aware of his actions and did not act, then they can be seen as enabling him to commit illegal acts. They had an economic incentive to uphold the standards that senior management has put in place, since that is part of their job responsibility. Ethically, they had a responsibility to senior management, their colleagues, and their direct reports. It was the responsibility of senior management to work with the supervisors, and it was up to senior management to work with the supervisors to see that rules and regulations were upheld.

The board of directors has an obligation to make sure that the employees of the Company act in accordance with the laws of the country they reside in. The board has an economic responsibility to the shareholders of stock in the Company. Ethically, the board must create rules of conduct and ethical standards and practice a rule by example. The board is a supportive, low-potential-threat stakeholder that will probably cooperate with the CEO in this case.

Where Is He Now?

"A lower court in France convicted Kerviel in October 2010 of forgery, breach of trust and unauthorized computer use for covering up bets worth nearly 50 billion

euros in 2007 and 2008. By the time his trades were discovered and made public, he had amassed losses of almost 5 billion euros on those bets", reported the Associated Press. He lost the subsequent appeal, the Paris Appeals Court upholding Kerviel's sentence in its entirety in 2012. He is currently serving a three-year prison sentence.

Questions for Discussion

1. Is Kerviel the only guilty one in this case with regard to his actions? Also, does the punishment fit the crime in this case? Explain both of your answers.
2. Should other individuals and the bank be held legally responsible and liable for Kerviel's actions? Why or why not? Explain.
3. Describe what you believe to have been Kerviel's personal and professional ethics. Use the terms from this chapter as well as your own reasoning.
4. Compare your personal and professional ethics to Kerviel's.
5. Explain how a stakeholder and issues analysis can help you understand this case.
6. What are the lessons students in accounting, business, and organizational studies fields can take away from this case?

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Case 5

Samuel Waksal at ImClone

Seeking Approval for Erbitux

For several years, ImClone, a biotechnology company, was a darling of Wall Street. Its stock price rose from less than $1 per share in 1994 to $72 a share in November 2001. "The whole time it was producing nothing for sale. It did generate some revenue through licensing agreements with other drug companies—signs that the pharmaceutical industry did think ImClone was on to something." ImClone focused on developing a cancer treatment drug called Erbitux. Erbitux is intended to make cancer treatment more effective by "targeting a protein called epidermal growth factor receptor (EGFR), which exists on the surface of cancer cells and plays a role in their proliferation."

In its 10-K Annual Report for the fiscal year ending December 31, 2001, ImClone described Erbitux as the company's "lead product candidate" and indicated that Erbitux had been shown in early stage clinical trials to cause tumor reduction in certain cases. ImClone had planned to market the drug in the United States and Canada with its development partner, Bristol-Myers Squibb. On September 19, 2001, ImClone announced that Bristol-Myers Squibb had paid $2 billion for the marketing rights to Erbitux and would codevelop and copromote Erbitux with ImClone.

ImClone was one of at least five pharmaceutical companies with EGFR drugs in mid- to late-stage testing. The winners at commercialization of a new drug class—such as EGFR—are the "companies that beat their rivals to market, since doctors tend to embrace the initial entries." Under this pressure, ImClone took a testing shortcut, using what is known as a single-armed study—one which is conducted without a control group. ImClone's use of the single-armed study failed to meet the U.S. Food and Drug Administration's (FDA) rigorous criteria for using the methodology.

Samuel Waksal, ImClone's cofounder and CEO at the time, was directly involved in coordinating and publicizing ImClone's efforts to develop Erbitux and to obtain FDA approval for it. On June 28, 2001, ImClone began the process of submitting a rolling application—called a Biologics License Application (BLA)—seeking FDA approval for Erbitux. On October 31, 2001, ImClone submitted to the FDA the final substantial portion of its BLA. The FDA had a 60-day period within which a decision had to be made concerning whether to accept the BLA for filing. The FDA had three options: (1) accept ImClone's BLA for filing; (2) accept the BLA for filing, but simultaneously issue a disciplinary review letter notifying ImClone that the BLA still had serious deficiencies that would need to be corrected before the BLA could be approved; or (3) refuse to approve the drug by issuing a Refusal to File letter (RTF). When the FDA issues a RTF, the applicant must file a new BLA to start the process over.

Samuel Waksal's Reaction to the Impending Refusal to File

On December 25, 2001, Bristol-Myers Squibb learned from a source at the FDA that the FDA would issue a RTF letter on December 28, 2001. On the evening of December 26, 2001, Waksal learned of the FDA's decision and attempted to sell 79,797 shares of ImClone stock that were held in his brokerage account with Merrill Lynch. He initially told his agent to transfer the shares to his daughter's account. The following morning he instructed his agent to sell the shares. When Waksal's agent called Merrill Lynch in order to sell the shares, the agent was told that the shares were restricted and could not be sold without the approval of ImClone's legal counsel. When Merrill Lynch refused to conduct the transaction, Waksal ordered his agent to transfer the shares to Bank of America and then sell them. Bank of America also refused to conduct the transaction, and the shares were never sold.

On December 26, 2001, Waksal contacted his father, Jack Waksal, informing him of the impending RTF. The next morning, Jack Waksal placed an order to sell 110,000 shares of ImClone stock. Jack Waksal also called Prudential Securities and placed an order to sell 1,336 shares of ImClone stock from the account of his daughter, Patti Waksal. On December 28, Jack Waksal sold another 25,000 shares of ImClone stock. When questioned by the staff of the Securities and Exchange Commission (SEC), Jack Waksal provided false and misleading explanations for these trades.

On the morning of December 27, 2001, before the stock market opened, Samuel Waksal had a telephone conversation with his daughter, Aliza. At that time, Waksal was Aliza's only means of support, and he had control of her bank and brokerage accounts. During their conversation, he directed her to sell all of her ImClone shares. Immediately after talking to her father, Aliza placed an order at 9 a.m. to sell 39,472 shares of ImClone stock. By selling her shares at that moment in time, she avoided $630,295 in trading losses.

On December 28, 2001, Waksal purchased 210 ImClone put option contracts, buying them through an account at Discount Bank and Trust AG in Switzerland. He sold all 210 put option contracts on January 4, 2002, which resulted in a profit of $130,130. Waksal also failed to file a statement disclosing a change of ownership of his ImClone securities as required by Section 16(a) of the Exchange Act and Rule 16a-3.

According to the SEC, Waksal violated several sections of the Securities Act when he attempted to sell his own ImClone Stock, when he illegally tipped his father about the FDA decision, when he caused Aliza to sell her shares of ImClone stock, and when he purchased ImClone put option contracts.

The Outcome for Samuel Waksal and ImClone

Waksal resigned as ImClone's CEO on May 21, 2002, and on June 12 was arrested for securities fraud and perjury. Two months later he was indicted for bank fraud, securities fraud, and perjury. On October 15, 2002, Waksal pleaded guilty to all of the counts in the indictment, except those counts based on allegations that he passed material, nonpublic information to his father. On March 3,

2003, he also pleaded guilty to tax evasion charges for failing to pay New York State sales tax on pieces of art he had purchased. On June 10, 2003, Waksal was sentenced to 87 months in prison and was ordered to pay a $3 million fine and $1.2 million in restitution to the New York State Sales Tax Commission. Waksal began serving his prison sentence on July 23, 2003.

Despite Waksal's actions, ImClone appears to have survived the scandal. Under the leadership of Daniel Lynch, ImClone's former chief financial officer and its current CEO, the company has staged a remarkable turnaround. Most of ImClone's 440 employees stayed with the company and helped Lynch revive it. Lynch says the employees stayed for one overpowering reason—they believed in Erbitux. As for himself, Lynch asserted that "What motivated me to get up in the morning was knowing that if I could get this drug approved, it would improve the lives of patients with cancer." Based on a clinical trial by Merck KGaA, ImClone's European marketing partner, the FDA, on February 12, 2004, "approved Erbitux for treating patients with advanced colon cancer that has spread to other parts of the body." Thus, Erbitux became ImClone's first commercial product.

Where Are They Now?

Waksal is currently making a comeback in the biotech industry. Since the scandal, ImClone has since been sold to Eli Lilly for a price of $6.5 billion in 2008. The next year, Waksal was caught up in the Martha Stewart Insider Trading scandal as well, and has since served jail time. Waksal's new company, Kadmon Corp., is his new biopharmaceutical firm; he plans to open a sister company in China on the Hong Kong Exchange.

Questions for Discussion

1. What might motivate an individual or a company to short-cut drug testing that is crucial for FDA approval?
2. Why did Samuel Waksal react as he did pursuant to learning that the FDA would not approve Erbitux?
3. Why were Samuel Waksal's actions unethical?

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3

STAKEHOLDER AND ISSUES MANAGEMENT APPROACHES

3.1 Stakeholder Theory and the Stakeholder Management Approach Defined

3.2 Why Use a Stakeholder Management Approach for Business Ethics?

3.3 How to Execute a Stakeholder Analysis

3.4 Negotiation Methods: Resolving Stakeholder Disputes

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6. The BP *Deepwater Horizon* Explosion and Oil Spill: Crisis and Aftermath
7. Mattel Toy Recalls
8. Genetic Discrimination

Notes

OPENING CASE

The oil company BP (formerly British Petroleum) leased/licensed the *Deepwater Horizon* oil rig, operated by Transocean and contracted by Halliburton, that exploded in flames in the Gulf of Mexico on the night of April 20, 2010.[1, 2] The result was 11 deaths, 17 injured, and hundreds of miles of beaches soiled. A "blowout preventer" (specialized valve) designed to prevent crude oil releases failed to activate.[3]

The factual events leading up to the BP blowout unearth a highly complex network of stakeholders, stakes, and circumstances, which though preventable, together culminated in the worst environmental disaster recorded in U.S. history. In March 2008, the U.S. Occupational Safety and Health Administration (OSHA) recorded on public record that BP had one of the worst safety records in its industry. After the explosion when the *Deepwater Horizon* sank, "a sea-floor oil gusher

flowed for 87 days, until it was capped on 15 July 2010."[4] The total oil spill was estimated at 210 million U.S. gallons. With all-out efforts by BP and a host of other organizations and crews, by September 2010, the entire well had been sealed, but the legal and ethical issues and stakeholder disputes had only begun. In 2013, over 2.7 million pounds of "oiled material" had been removed from the Louisiana coast and tar balls were reported daily on Alabama and Florida beaches.

Different phases of the trials are ongoing.[5] BP has already admitted guilt in 2012 to 14 criminal charges that included manslaughter and "negligence in misreading important tests before the explosion." The company agreed to pay $4.5 billion in fines and penalties. "Four current or former employees also face criminal charges. The company has spent more than $42 billion on cleaning up the environment and compensating victims. People and businesses continue to file claims for damages, and there is no cap to the damages."[6]

The Justice Department and Judge Barbier are overseeing and managing a latter part of the trial between the plaintiffs (Transocean, Halliburton, the states of Louisiana and Alabama, and private plaintiffs) and BP (with its partner, Anadarko Petroleum). The main issue at this point in the case that the plaintiffs must prove is whether or not a total 4.2 million barrels of oil was discharged as a result of the oil rig exploding into the sea 87 days after the explosion. That amount of oil is the equivalent of nearly one-quarter of all the oil consumed in the United States in one day. Plaintiffs allege that BP's failure of preparation caused the crisis and aftermath of oil flow. BP is defending whether or not it was prepared for a blowout and if its response was adequate once the oil started leaking.[7]

Stakeholders in this crisis number in the thousands. In the federal government alone there are the Departments of Energy, Interior, Justice, members of Congress, and even President Obama–who met with BP executives in June 2010 and persuaded them "to create a $20 billion fund to compensate residents and businesses for losses resulting from the spill."[8] Obama also announced plans to empower the Minerals Management Service to oversee offshore drilling. Other key stakeholders include BP employees and their families, BP's partners, and the plaintiffs.

BP agreed to a settlement involving literally thousands of individuals affected by the spill in 2012 totaling $7.8 billion–the amount which BP would have to pay was not capped, however.[9] Over 200,000 individuals and businesses were paid $6.1 billion through the Gulf Coast Claims Facility. Add to this number the state governments and agencies affected by the spill, the lawyers on both sides of the case, insurance companies, auditors, and competitors, all of whom are also stakeholders. In addition, the response and aftermath cleanup "involved thousands of boats, tens of thousands of workers, and millions of feet of containment boom."

BP's then chief executive officer (CEO) Tony Hayward defended BP against accusations that the company was not prepared and that it cut corners on the design of the well, and then attempted to escape responsibility for the consequences. He was replaced by Robert Dudley, BP's managing director after the blowout, when Hayward was criticized for minimizing the scale of the spill, and for making such remarks as, "There's no one who wants this thing over more than I do. I'd like my life back"—which particularly offended members of the workers' families who died in the explosion. His presence at a yacht race in June after the spill reportedly contributed to a sense of insensitivity.[10]

This crisis will be studied and analyzed for years to come. The human, political, economic, environmental, and social costs were enormous. "Tens of thousands of families have been affected by the spill, whether they work in the fishing industry, tourism, or oil. The area of the spill supplies 40% of seafood in the U.S., and the leaked oil put fishermen, crabbers and oystermen out of work. Some of these workers were hired to help contain the spill and clean the beaches; others filed for unemployment benefits."[11] To date, BP as a "supermajor" in its industry has moved from the highest earnings per barrel to the lowest, falling behind Shell, Exxon, and Chevron Corp.[12] Nevertheless, according to CEO Dudley, the company has increased its investment "in exploration and projects annual capital spending over the next several years to be $24 billion to $27 billion—at least 25% higher than 2011 levels as the company pours cash into projects in Angola, Azerbaijan, Indonesia and elsewhere."[13]

3.1 Stakeholder Theory and the Stakeholder Management Approach Defined

The BP *Deepwater Horizon* oil spill is a complex crisis not limited to the financial, economic, and corporate interests involved. Since numerous people, businesses, and the environment were affected, and 11 workers lost their lives, an analysis that also encompasses ethical and moral considerations is required.

Stakeholder theory is best described by R. Edward Freeman—its modern founder. "My thesis is that I can revitalize the concept of managerial capitalism by replacing the notion that managers have a duty to stockholders with the concept that managers bear a fiduciary relationship to stakeholders. Stakeholders are those groups who have a stake in or claim on the firm. Specifically I include suppliers, customers, employees, stockholders, and the local community, as well as management in its role as agent for these groups. . . . Each of these stakeholder groups has a right not to be treated as a means to some end, and therefore must participate in determining the future direction of the firm in which they have a stake."[14] Freeman and his collaborators state that it is "a mistake to see stakeholder theory as a specific theory with a single purpose. Researchers would do well to see stakeholder theory as a set of shared ideas

that can serve a range of purposes within different disciplines and address different questions."[15]

The *stakeholder management approach* is based on a related instrumental theory that argues "a subset of ethical principles (trust, trustworthiness, and cooperativeness) can result in significant competitive advantage."[16] This approach, then, enables researchers and practitioners to use analytical concepts and methods for identifying, mapping, and evaluating corporate strategy with stakeholders. We refer to the use of this instrumental approach in stakeholder theory as "stakeholder analysis."

The stakeholder management approach, including frameworks for analyzing and evaluating a corporation's relationships (present and potential) with external groups, aims ideally at reaching "win–win" collaborative outcomes. Here, "win–win" means making moral decisions that benefit the common good of all constituencies within the constraints of justice, fairness, and economic interests. Unfortunately, this does not always happen. There are usually winners and losers in complex situations where there is a perceived zero-sum game (i.e., a situation in which there are limited resources, and what is gained by one person is necessarily lost by the other).

Scholars and consultants, however, have used the stakeholder management approach as a means for planning and implementing collaborative relationships to achieve win–win outcomes among stakeholders.[17] Structured dialogue facilitated by consultants is a major focus in these collaborative communications. The aim in using the stakeholder approach as communication strategy is to change perceptions and "rules of engagement" to create win–win outcomes.

A stakeholder management approach does not have to result from a crisis, as so many examples from ethics literature and the news provide. It can also be used as a planning method to anticipate and facilitate business decisions, events, and policy outcomes. A stakeholder analysis is not only limited to publicly traded for-profit enterprises, but also applies to non-profit organizations: "Stakeholder theorists clearly indicate that their theory is intended to more than merely for-profit corporations."[18]

A stakeholder management approach also begins, as indicated in Chapter 1, by asking what external forces in the general environment are affecting an organization. This context can often provide clues to responses by stakeholders to opportunities, crises, and extraordinary events. Corporate scandals revealed after the Enron crisis that there were several factors in the general environment that were at play in addition to certain corporate executives' greed. For example, the dotcom technology bubble leading up to the year 2000 created a financial environment where investment funds followed innovative ideas in exorbitant and exuberant ways. Investment banks loaned large amounts to Enron and other companies without due diligence. Stock analysts lied and encouraged deceptive investing from the public. Boards of directors abandoned their fiscal responsibilities, as did large accounting firms like Arthur Andersen, which is no longer in existence. The general legal and enforcement environment during the 1990s appeared indifferent to monitoring corporate activities and protecting shareholders. A similar general environment

with low-to-nonexistent government regulation followed, culminating in the 2008 subprime lending crisis that sent the global economy reeling. Next we define the term "stakeholder."

Stakeholders

A *stakeholder* is "any individual or group who can affect or is affected by the actions, decisions, policies, practices, or goals of the organization."[19] We begin by identifying the *focal stakeholder.* This is the company or group that is the focus or central constituency of an analysis.

The *primary stakeholders* of a firm include its owners, customers, employees, and suppliers. Also of primary importance to a firm's survival are its stockholders and board of directors. The CEO and other top-level executives can be stakeholders, but in the stakeholder analysis they are generally considered actors and representatives of the firm. In this chapter's opening case, BP's CEO and top-level team are focal stakeholders. Coalitional focal stakeholders that may also be connected to BP primary stakeholders include owners, customers, employees, and, in this case, Chinese vendors and suppliers.

Secondary stakeholders include all other interested groups, such as the media, consumers, lobbyists, courts, governments, competitors, the public, and society. Halliburton and Transocean were considered as "secondary stakeholders" by then CEO and other officers; after the spill, these collaborators became plaintiffs. Control and quality of products and services can be diminished and/or lost with outsourced and licensing relationships if proper monitoring and management is absent. One final report on this case suggested that the real root of the problem was BP's own laissez-faire approach to safety, even though spokespersons from BP denied this allegation.[20]

Stakes

A *stake* is any interest, share, or claim that a group or individual has in the outcome of a corporation's policies, procedures, or actions toward others. Stakes may be based on any type of interest. The stakes of stakeholders are not always obvious. The economic viability of competing firms can be at stake when one firm threatens entry into a market. The physical environment, employees' lives, and the health and welfare of communities can be at stake when corporations like BP either relax or do not have in place proper equipment, safety standards, and emergency plans for crises.

Stakes also can be present, past, or future oriented. For example, stakeholders may seek compensation for a firm's past actions, as occurred when lawyers argued that certain airlines owed their clients monetary compensation after having threatened their emotional stability when pilots announced an impending disaster (engine failure) that, subsequently, did not occur. Stakeholders may seek future claims; that is, they may seek injunctions against firms that announce plans to drill oil or build nuclear plants in designated areas or to market or bundle certain products in noncompetitive ways.

3.2 Why Use a Stakeholder Management Approach for Business Ethics?

The stakeholder management approach is a response to the growth and complexity of contemporary corporations and the need to understand how they operate with their stakeholders and stockholders. Stakeholder theory argues that corporations should treat all their constituencies fairly and that doing so can enable the companies to perform better in the marketplace.[21] "If organizations want to be effective, they will pay attention to all and only those relationships that can affect or be affected by the achievement of the organization's purposes."[22] Although stakeholder theory includes a fiduciary dimension by nature of its intent, as Freeman was quoted as saying above, we apply this theory in ways that use ethical principles such as justice, utilitarianism, rights, and universalism to individual stakeholders and their interactions with each other and corporations.

This chapter applies the stakeholder management approach not only in its theoretical form, but also as a practical method to analyze how companies deal with their stakeholders. We therefore use the term "stakeholder analysis" (which is part of stakeholder management) to identify strategies, actions, and policy results of firms in their management of employees, competitors, the media, courts, and stockholders. Later in the chapter, we introduce "issues management" as another set of methods for identifying and managing stakeholders. We present issues management and stakeholder theory as complementary theories that use similar methods, as we show later. Starting with a major issue or opportunity that a company faces is a helpful way to begin a stakeholder analysis.

A more familiar way of understanding corporations is the *stockholder approach,* which focuses on financial and economic relationships. By contrast, a stakeholder management approach is a normative and instrumental approach that studies actors' interests, stakes, and actions.[23] The stakeholder management approach takes into account nonmarket forces that affect organizations and individuals, such as moral, political, legal, and technological interests, as well as economic factors.

Underlying the stakeholder management approach is the ethical imperative that mandates that businesses in their fiduciary relationships to their stockholders: (1) act in the best interests of and for the benefit of their customers, employees, suppliers, and stockholders; and (2) respect and fulfill these stakeholders' rights. One study concluded that "multiple objectives—including both economic and social considerations—can be and, in fact, are simultaneously and successfully pursued within large and complex organizations that collectively account for a major part of all economic activity within our society."[24]

Stakeholder Theory: Criticisms and Responses

The dominant criticism of stakeholder theory by some scholars is that corporations should serve only stockholders since they own the coporation.[25] It is important to observe criticisms of stakeholder theory and responses to them

in order to understand the purpose of and benefits provided by stakeholder theory. The following criticisms have been offered by scholars: stakeholder theory (1) negates and weakens fiduciary duties that managers owe to stockholders, (2) weakens the influence and power of stakeholder groups, (3) weakens the firm, and (4) changes the long-term character of the capitalist system.[26] Ethically, these arguments are based on property and implied contract rights, and on fiduciary duties and responsibilities of managers to stockholders.

Critics claim that some stakeholder groups' power can be weakened by stakeholder theory by treating all stakeholders equally—as stakeholder theory suggests. For example, labor unions can be avoided, hurt, or even eliminated. Corporations can also be weakened in their pursuit of profit if they attempt to serve all stakeholders' interests. The corporation cannot be all things to all stakeholders and protect stockholders' fiduciary interest. Finally, critics who claim that stakeholder theory changes the long-term character of capitalism argue that: (1) corporations have no responsibility by law other than to their stockholders, since the market disciplines corporations anyway; and (2) stakeholder theory permits some managers to "game" corporations by arguing that they are protecting some stakeholder interests, even if interests of others are harmed. Some more leftist thinkers also criticize advocates of stakeholder theory as being naive and utopian. These critics claim that well-intentioned "do-gooders" ignore or mask the reality of capital labor relationships through simplistic notions in stakeholder theory such as "participation," "empowerment," and "realizing human potential."[27]

Despite these criticisms, stakeholder theory continues to be popular and widely used. As noted earlier in this chapter, societies and economies involve market and nonmarket interests of diverse stakeholders as well as stockholders. To understand and effect responsible corporate strategies, methods that include different players and environmental factors—not just stockholders or financial interests—are required. We also live in a post-Enron world. Some officers in corporations can engage in illegal and unethical practices with investors' funds and assets. Stakeholder theory addresses these realities. The following points also respond to some of the above criticisms. First, stakeholder theory does offer advantages; for example, Heugens and Van Riel (2002) present evidence showing that stakeholder theory may result in both organizational learning and societal legitimacy. Secondly, Key's (1999) stakeholder theory of the firm,[28] summarized by Mitchell, Agle, and Wood (1997),[29] states: "stakeholder theory must account for power and urgency as well as legitimacy, no matter how distasteful or unsettling the results. Managers must know about groups in their environment that hold power and intend to impose their will upon the firm. Power and urgency must be attended to if managers are to serve the legal and moral interests of legitimate stakeholders."

The ethical dimension of stakeholder theory is based on the view that profit maximization is constrained by justice, and that regard for individual rights should be extended to all constituencies that have a stake in a business, and that organizations are not only "economic" in nature, but can also act in socially responsible ways. To this end, companies *should* act in socially respon-

sible ways, not only because it's the "right thing to do," but also to ensure their legitimacy.[30]

3.3 How to Execute a Stakeholder Analysis

Stakeholder analysis is a pragmatic way of identifying and understanding multiple (often competing) claims of many constituencies. As part of a general stakeholder approach, stakeholder analysis is a method to help understand the relationships between an organization and the groups with which it must interact. Each situation is different and therefore requires a map to guide strategy for an organization dealing with groups, some of whom may not be supportive of issues, such as outsourcing jobs. The aim here is to familiarize you with the framework so that you can apply it in the classroom and to news events that appear in the press and in other media. Even though you may not be an executive or manager, the framework can enable you to see the "big picture" of complex corporate dealings, and apply ethical reasoning and principles when analyzing strategies used by managers and different stakeholders.

Taking a Third-Party Objective Observer Perspective

In the following discussion, you are asked to assume the role of a CEO of a company to execute a stakeholder analysis. However, it is recommended that you take the role of "third-party objective observer" when doing a stakeholder analysis. Why? In this role, you will need to suspend your belief and value judgments in order to understand the strategies, motives, and actions of the different stakeholders. You may not agree with the focal organization or CEO whom you are studying. Therefore, the point is to be able to see all sides of an issue and then objectively evaluate the claims, actions, and outcomes of all the parties. Being more objective helps determine who acted responsibly, who won and who lost, and at what costs.

Part of the learning process in this exercise is to see your own blind spots, values, beliefs, and passions toward certain issues and stakeholders. Doing an in-depth stakeholder analysis with a group enables others to see and comment on your reasoning. For the next section, however, take the role of a CEO so you can get an idea of what it feels like to be in charge of directing an organization-wide analysis.

Role of the CEO in Stakeholder Analysis

Assume for this exercise that you are the CEO, working with your top managers, in a firm that has just been involved in a major controversy of international proportions. The media, some consumer groups, and several major customers have called you. You want to get a handle on the situation without reverting to unnecessary "firefighting" management methods. A couple of your trusted staff members have advised you to adopt a planning approach quickly while responding to immediate concerns and to understand the "who,

what, where, when, and why" of the situation before jumping to "how" questions. Your senior strategic planner suggests you lead and participate in a stakeholder analysis. What is the next step?

The stakeholder analysis is a series of steps aimed at the following tasks:[31]

1. Map stakeholder relationships.
2. Map stakeholder coalitions.
3. Assess the nature of each stakeholder's responsibilities.
4. Assess the nature of each stakeholder's power.
5. Construct a framework of stakeholder moral responsibilities and interests.
6. Develop specific strategies and tactics.
7. Monitor shifting coalitions.

Each step is described in the following sections. Let's explore each one and then apply them in our continuing scenario example.

Step 1: Map Stakeholder Relationships

In 1984, R. Edward Freeman offered questions that help begin the analysis of identifying major stakeholders (Figure 3.1). The first five questions in the figure offer a quick jump-start to the analysis. Questions 6 through 9 may be used in later steps, when you assess the nature of each stakeholder's interest and priorities.

Let's continue our example with you as CEO. While brainstorming about questions 1 through 5 with employees you have selected who are the most knowledgeable, current, and close to the sources of the issues at hand, you may want to draw a stakeholder map and fill in the blanks. Note that your stake-

Figure 3.1

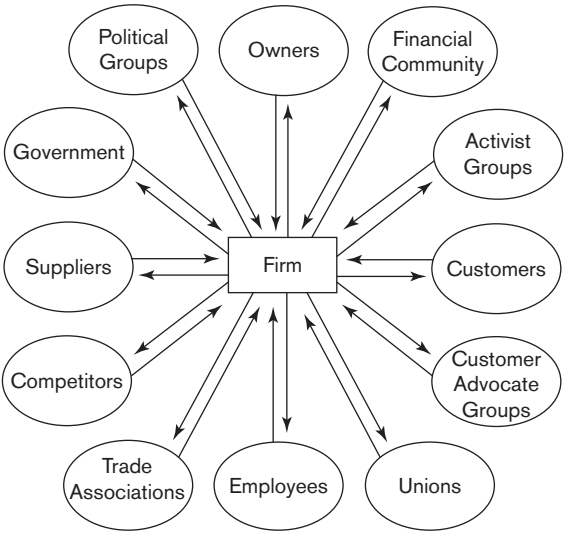
Sample Questions for Stakeholder Review

1. Who are our stakeholders currently?
2. Who are our potential stakeholders?
3. How does each stakeholder affect us?
4. How do we affect each stakeholder?
5. For each division and business, who are the stakeholders?
6. What assumptions does our current strategy make about each important stakeholder (at each level)?
7. What are the current "environmental variables" that affect us and our stakeholders (initiation, GNP, prime rate, confidence in business [from polls], corporate identity, media image, and so on)?
8. How do we measure each of these variables and their impact on us and our stakeholders?
9. How do we keep score with our stakeholders?

Source: Freeman, R. Edward. (1984). *Strategic management: A stakeholder approach,* 242. Boston: Pitman. Reproduced with permission of the author.

Figure 3.2

Stakeholder Map of a Large Organization



Source: Freeman, R. Edward. (1984). *Strategic management: A Stakeholder approach,* 25. Boston: Pitman. Reproduced with permission of the author.

holder analysis is only as valid and reliable as the sources and processes you use to obtain your information. As a CEO in this hypothetical scenario, which is controversial, incomplete, and in which questionable issues arise, you may wish to go outside your immediate planning group to obtain additional information and perspective. You should therefore identify and complete the stakeholder map (Figure 3.2), inserting each relevant stakeholder involved in the particular issue you are studying.

For example, if you were examining the BP spill—and you were not the CEO of that company—you would place BP and the then CEO Tony Hayward—later replaced by Robert Dudley—in the center (or focal) stakeholder box, then continue identifying the other groups involved: Halliburton, Transocean, employees who were victims and those immediately endangered by the spill, shareholders (members of the lawsuit), affected community victims (families), affected community businesses, the U.S. government (the Departments of Justice and the Interior), the U.S. Congress, President Obama, suppliers and distributors, competitors, among others. In completing a stakeholder map, include real groups, individuals, and organizations—issues are not part of the formal stakeholder map.

Note that in Figure 3.2 the reciprocal arrows represent enacted major strategies and tactics between each stakeholder and the focal stakeholder.

Step 2: Map Stakeholder Coalitions

After you identify and make a map of the stakeholders who are involved with your firm in the incident you are addressing, the next step is to determine

and map any coalitions that have formed. Coalitions among stakeholders form around stakes that they have—or seek to have—in common. Interest groups and lobbyists sometimes join forces against a common "enemy." Competitors also may join forces if they see an advantage in numbers. Mapping actual and potential coalitions around issues can help you, as the CEO, anticipate and design strategic responses toward these groups before or after they form.

Step 3: Assess the Nature of Each Stakeholder's Responsibilities

Next you need to identify the nature of each stakeholder's interests and responsibilities in a particular situation. Since each stakeholder has a stake, interest, or claim in the process and outcomes of the situation, opportunity, controversy, or crisis, it is important to assess the nature of the focal organization's responsibilities toward each stakeholder group. As Figure 3.3, which is based on Archie Carroll's work on the Pyramid of Corporate Social Responsibility and the Moral Management of Organizational Stakeholders, illustrates, addressing the legal, economic, ethical, and voluntary nature of a company's responsibility toward owners, customers, employees, community groups, the public, government, and victims brings a moral awareness to the CEO of the focal company. For example, in 2014 the pharmacy chain CVS banned the sale of tobacco products from its 7,600 stores, a decision made with the expressed intent of helping create a smoke-free generation. With regard to Figure 3.3, this voluntary decision may affect CVS's short-term profits, but it takes an ethical

Figure 3.3

Nature of Focal Organization's Ethical Responsibilities

Stakeholders	Economic	Legal	Ethical	Voluntary
Owners				
Leaders and Managers				
Employees				
Customers				
Suppliers				
Communities				
Competitors				
Suppliers				
Media				
Government				
Public				
Victims				
Other?				

Source: Adapted from Carroll, A. (July–August 1991). The pyramid of corporate social responsibility: Toward the moral management of organizational stakeholders. *Business Horizons, 34 (4),* 44.

stand that influences all its stakeholders and stockholders. This step is not limited to the CEO; other stakeholders would benefit from using it. With regard to the BP situation, had the CEO and his core team completed this exercise and acted responsibly, he may not have lost his job.

For example, BP's CEO may see the firm's *economic responsibility* to the owners (as stakeholders) as "preventing as many costly lawsuits as possible." *Legally,* the CEO may want to protect the owners and the executive team from liability and damage; this would entail proactively negotiating disputes outside the courts, if possible, in a way that is equitable to all. *Ethically,* the CEO may keep the company's stockholders and owners up to date regarding his or her ethical thinking and strategies to show responsibility toward all stakeholders. At stake is the firm's reputation as well as its profitability. In the case of BP and other crises, the CEO's job and future career with the company can be at risk. Missteps in communicating with the media and visible stakeholders, and showing insensitivity to victims or the situation can cause an executive to lose his/her job during a crisis, as was the case at BP.

Step 4: Assess the Nature of Each Stakeholder's Power

This part of the analysis asks, "What's in it for each stakeholder? Who stands to win, lose, or draw over certain stakes?" Eight types of power that different stakeholders exert and which you can use in your analysis include (1) *voting power* (the ability of stakeholders to exert control through strength in numbers), (2) *political power* (the ability to influence decision-making processes and agendas of public and private organizations and institutions), (3) *economic power* (the ability to influence by control over resources—monetary and physical), (4) *technological power* (the ability to influence innovations and decisions through uses of technology), (5) *legal power* (the ability to influence laws, policies, and procedures), (6) *environmental power* (the ability to impact nature), (7) *cultural power* (the ability to influence values, norms, and habits of people and organizations), and (8) *power over individuals and groups* (the ability to influence particular, targeted persons and groups through different forms of persuasion).[32] The BP example suggests that shareholders, members of Congress, and individual constituents have voting power over BP's policies, and officers' jobs and responsibilities. The president of the United States, government regulatory agencies, consumers, stock market analysts, and investors all exert economic power over BP in this situation. The U.S. government, regulatory agencies, and interest groups also exert political power over BP's operating and manufacturing policies, processes, and products.

Note that power and influence are exerted in two-way relations: BP toward its stakeholders, and each stakeholder toward BP on a given issue. For example, owners and stockholders can vote on the firm's decisions regarding a particular issue or opportunity, such as BP's future drilling plans. On the other hand, federal, state, and local governments can exercise their political power by voting on BP's legal obligations toward consumers. New legislation may emerge with regard to the regulation of BP's outsourcing and quality-control methods. In return, consumers can exercise their economic power by boycotting BP's products or buying from other companies. What other sources of stakeholder power exist in this case?

Step 5: Construct a Framework of Stakeholder Moral Responsibilities and Interests

After you map stakeholder relationships and assess the nature of each stakeholder's interest and power, the next step is to identify the moral obligations your company has to each stakeholder.

Chapter 2 explained the ethical principles and guidelines that can assist in this type of decision making. For purposes of completing this matrix, ethical decision making of company representatives can refer to the following ethical principles: *utilitarianism* (weighing costs and benefits; "ends justifying means"); *universalism* (showing respect and concern for human beings—"means count as much as ends"); *rights* (recognizing individual liberties and privileges under laws and constitutions); *justice* (observing the distribution of burdens and benefits of all concerned). *Voluntarily* (i.e., acting freely and from one's own accord), the CEO may advise shareholders to show responsibility by publicly announcing their plans for resolving the issue of the firm's "next steps." This can also be done in more open and conscientious marketing activities as well as in a consciously responsible distribution of products.

This part of the analysis lays the foundation for developing specific strategies toward each stakeholder you have identified. Notice that developing strategies first preempts and may omit putting "first things first," in this case this means meeting your moral responsibilities to those affected in the situation, and not protecting or promoting profit first and at any costs. Although there is a fiduciary responsibility toward your stockholders, you may discover that you can lose your company (bankruptcy) and its assets, including your job, if you do not also attend to powerful noneconomic interests—customers, victims and their families' lives in crisis situations, communities' needs, the media's attacks, and legitimacy with the general public and government.

Step 6: Develop Specific Strategies and Tactics

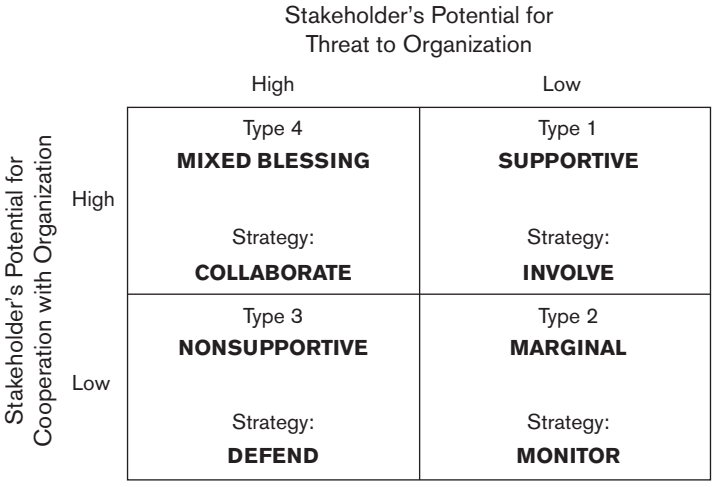
Using the results from the preceding steps, you can now proceed to outline the specific strategies and tactics you wish to use with each stakeholder. If you are a CEO using this framework, you can use Figure 3.4 along with the previous frameworks in this section to help articulate strategies to employ with different stakeholders.[33]

The typology of organizational stakeholders in Figure 3.4 shows two dimensions: potential for threat and potential for cooperation. Note that stakeholders can move among the quadrants, changing positions as situations and stakes change. Generally, officers of a firm in controversial situations, or situations that offer significant opportunities for an organization, try to influence and move stakeholders toward type 1, the *Supportive* stakeholder with a low potential for threat and high potential for cooperation. Here the strategy of the focal company is to *involve* the supportive stakeholder. Think of both internal and external stakeholders who might be supportive and who should be involved in the focal organization's strategy.

In contrast, type 3, the *Nonsupportive* stakeholder, who shows a high potential for threat and a low potential for cooperation, represents an undesirable stance from the perspective of the influencer. The suggested strategy in

Figure 3.4

Diagnostic Typology of Organizational Stakeholders



Source: Savage, G. T., Nix, T. H., Whitehead, C. J., and Blair, J. D. (1991). Strategies for assessing and managing organizational stakeholders. *Academy of Management Executive, 5,* 65. © 1991 Academy of Management. Reproduced with permission of Academy of Management in the format Textbook via Copyright Clearance Center.

this situation calls for the focal organization to *defend* its interests and reduce dependence on that stakeholder.

A type 4 stakeholder is a *Mixed Blessing,* with a high potential for both threat and cooperation. This stakeholder calls for a *collaborative* strategy. In this situation, the stakeholder could become a Supportive or Nonsupportive type. A collaborative strategy aims to move the stakeholder to the focal company's interests.

Finally, type 2 is the *Marginal* stakeholder. This stakeholder has a low potential for both threat and cooperation. Such stakeholders may not be interested in the issues of concern. The recommended strategy in this situation is to *monitor* the stakeholder, to "wait and see" and minimize expenditure of resources, until the stakeholder moves to a Mixed Blessing, Supportive, or Nonsupportive position.

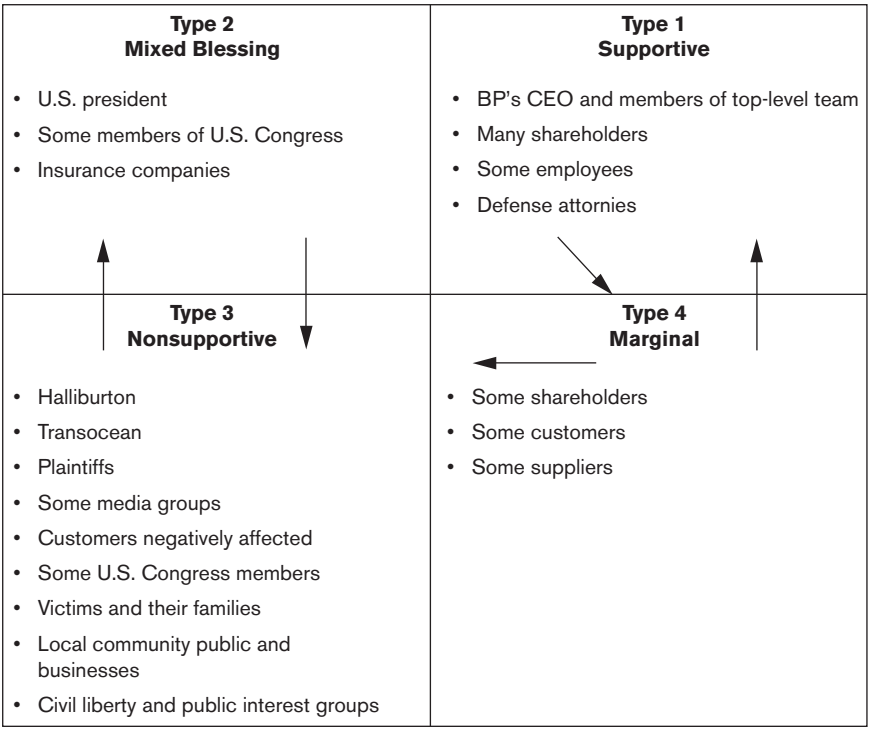
With regard to this chapter's opening case, had you been the BP CEO at that time, along with your staff after the explosion, you would have decided what strategy to pursue with regard to addressing the crisis. The nature of that strategy would have determined who would be the supporters and nonsupporters of BP's decisions. If you had chosen to deny and avoid responsibility for the explosion, or to blame the companies who were outsourced and running those projects, you may have found that your supporters would have been fewer and you may have realized that an avoidance, denial, and/or blame strategy would have pushed more stakeholders to the Nonsupportive space in Figure 3.5. Nonsupportive stakeholders would be those who sought

but did not find support and truthfulness from BP's officers with regard to owning responsibility, offering apologies, and then providing immediate help. Therefore, families of victims of the explosion—who appeared in the media, disgruntled and shocked employees from the rig who survived the explosion, community inhabitants in the vicinity of the oil spill, and others would be Nonsupportive. Who else would you add to those in opposition to BP at the time of the crisis, shortly afterward, and even a year, two or three down the road? By systematically completing this exercise through brainstorming with others who would be truthful with you, you, as a CEO in a crisis, can—before you react—create a broader, more objective and socially responsible picture of and response to the situation. At stake in such cases as the BP spill is the company's survival and reputation.

Figure 3.5 presents an example of the typology in Figure 3.4, using the BP oil spill case as an example. It is important to insert specific names of groups and individuals when doing an actual analysis. Indicate other stakeholders who might be or were influenced by BP's decision to outsource and recall products. Using your "third-party objective observer" perspective, you

Figure 3.5

Diagnostic Typology of Stakeholders for BP Corporation



can determine the movement among stakeholder positions using the arrows in the figure: Who influenced whom, by what means, and how over time? As you look at Figure 3.5, ask yourself: Do I agree with this figure as it is completed? Who is likely to move from Supportive to Nonsupportive? Or from a Mixed Blessing position to a Nonsupportive or Supportive one? Why? How? Support your logic and defend your position.

From the point of view of the focal stakeholder, if you were CEO, you would develop specific strategies and keep the following points in mind:

1. Your goal is to create a socially responsible, win–win set of outcomes, if possible. However, this may mean economic costs to your firm if, in fact, members of your firm are responsible to certain groups for harm caused as a consequence of your actions.
2. Ask: "What is our business? Who are our customers? What are our responsibilities to the stakeholders, to the public, and to the firm?" Keep your values, mission, and responsibilities in mind as you move forward.
3. Consider probable consequences of your actions. For whom? At what costs? Over what period? Ask: "What does a win–win situation look like for us?"
4. Keep in mind that the means you use can be important as the ends you seek; that is, how you approach and treat each stakeholder can be as important as what you do.

Specific strategies now can be articulated and assigned to corporate staff for review and implementation. Remember, social responsibility is a key variable; it is as important as the economic and political factors of a decision because social responsibility is linked to costs and benefits in other areas. At this point, you can ask to what extent your strategies are just and fair and consider the welfare of the stakeholders affected by your decision.

Executives use a range of strategies, especially in long-term crisis situations, to respond to external threats and stakeholders. Their strategies often are short-sighted and begin as a defensive move. When observing and using a stakeholder analysis, question why executives respond to their stakeholders as they do. Following the questions and methods in this chapter systematically will help you understand why key stakeholders respond as they do.

Step 7: Monitor Shifting Coalitions

Because time and events can change the stakes and stakeholders, and their strategies, you need to monitor the evolution of the issues and actions of the stakeholders using Figure 3.4. Tracking external trends and events and the resultant stakeholder strategies can help a CEO and his or her team act and react accordingly. This is a dynamic process that occurs over time and is affected by strategies and actions that you, as CEO, and your team direct with each stakeholder group as events occur. Your decisions are influenced by how effective certain stakeholders respond (or counteract) you and your team's strategies and actions. As CEO, you would typically follow a utilitarian ethic of weighing costs and benefits of all your strategies and actions toward each major stake-

holder group, keeping your company's best interests in mind. However, neglecting the public, common good of all your stakeholders also affects your bottom line. If you followed a universalistic ethic in the BP case, you might attempt to address concern and apologies to those who were harmed and condolences to the families of those who died in the explosion and aftermath of the disaster. You would have taken immediate action by offering factual information regarding what happened and why and what the company intended to do to resolve the crisis. Ethics is—should be—an integral part of every corporation's and organization's goals, objectives, strategies, and actions that affect other people. A question in the stakeholder analysis offered here is: What ethical principle(s)—if any—did the CEO of BP follow, and why, given the pressures from different stakeholders?

Summary of Stakeholder Analysis

You have now completed a basic stakeholder analysis and should be able to proceed with strategy implementation in more realistic, thoughtful, interactive, and responsible ways. The stakeholder approach should involve other decision makers inside and outside the focal organization.

Stakeholder analysis provides a rational, systematic basis for understanding issues and the "ethics in action" involved in complex relationships between an organization, its leaders, and constituents. It helps decision makers structure strategic planning sessions and decide how to meet the moral obligations of all stakeholders. The extent to which the resultant strategies and outcomes are moral and effective for a firm and its stakeholders depends on many factors, including the values of the firm's leaders, the stakeholders' power, the legitimacy of the actions, the use of available resources, and the exigencies of the changing environment.

3.4 Negotiation Methods: Resolving Stakeholder Disputes

Disputes are part of stakeholder relationships. Most disputes are handled in the context of mutual trusting relationships between stakeholders; others move into the legal and regulatory system.[34] Disputes occur between different stakeholder levels: for example, between professionals within an organization, consumers and companies, business to business (B2B), governments and businesses, and among coalitions and businesses. It is estimated that Fortune 500 senior human resource (HR) executives are involved in legal disputes 20% of their working time. Also, managers generally spend 30% of their time handling conflicts. The hidden cost of managing conflicts between and among professionals in organizations can result in absenteeism, turnover, legal costs, and loss of productivity.[35] U.S. retail e-commerce sales in the fourth quarter of 2011 were $51.4 billion, up 15.5% from 2010. With that volume, there will be business disputes. A study by the American Arbitration Association surveying 100 senior executives of Fortune 1000 companies found that:

1. Two out of three executives were concerned about B2B e-commerce disputes with major suppliers and 50% of surveyed executives noted that this type of dispute would significantly impact their business.

2. More than 50% noted that the shift to e-commerce will create new and/or different types of stakeholder disputes, with 64% of surveyed executives reporting their companies did not yet have a plan in place to deal with these disputes.

3. 70% agreed that specific guidelines are needed in order to manage e-commerce disputes, and one in four executives noted that their company did nothing to prevent e-commerce disputes.[36]

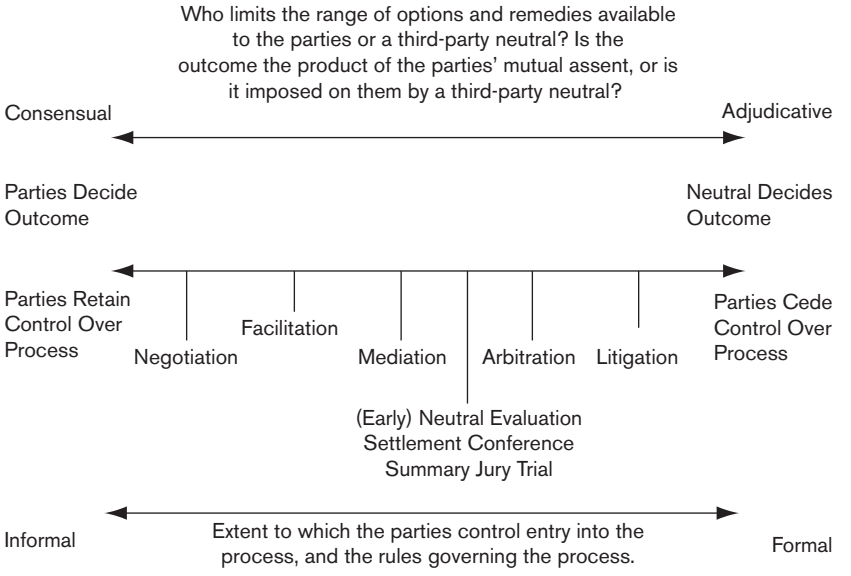
Stakeholder conflict and dispute resolution methods are clearly necessary.

Stakeholder Dispute Resolution Methods

Dispute resolution is an expertise also known as alternative dispute resolution (ADR). Dispute resolution techniques cover a variety of methods intended to help potential litigants resolve conflicts. The methods can be viewed on a continuum ranging from face-to-face negotiation to litigation, as Figure 3.6

Figure 3.6

The ADR Continuum



Source: Erickson, S. and Johnson, M. (January 27, 2012). ADR techniques and procedures flowing through porous boundaries: Flooding the ADR landscape and confusing the public. http://www.mediate.com/pdf/ADR%20Techniques%20and%20Procedures%20Flowing%20Through%20Porous%20Boundaries-%20Flooding%20the%20ADR%20Landscape%20and%20Confusing%20the%20Public%20(Revised,%20January%2027,%202012).pdf, accessed February 11, 2014.

illustrates. Advocates of alternative resolution methods argue that litigation need not be the standard for evaluating other dispute techniques.[37]

Figure 3.6 illustrates the degree to which disputing parties give up control of the process and outcome to a neutral third party. The left side of the continuum is based on consensual, informal dispute resolution methods. Negotiating, facilitation, and some mediation are methods where the parties maintain control over the conflict resolution process. Moving to the right side of the spectrum (adjudicative), disputing parties give up control to third-party arbitrators and then litigators (courts, tribunals, and binding arbitration). For example, with regard to outsourcing issues discussed earlier in the chapter, most companies have the authority to make outsourcing decisions. However, with regard to outsourced government contractors, for example, control over who and what types of contracts will be used is more complicated. For example, when the effort to start rebuilding Iraq after the invasions were over, Congress debated the use of external contractors for those projects. Halliburton received several exclusive outsourced contracts toward that effort. Congress used the National Defense Authorization Act for Fiscal Year 2005 to enable civil service employees in the Departments of Defense and Homeland Security, the Internal Revenue Service, and the Pentagon to control the use of external contractors. It was reported recently that "Between 2003 and 2008, Congress estimated that the United States had spent $100 billion on contractors in Iraq, or one dollar out of every five spent on the Iraq War at the time. Today, assuming a conservative estimate of $800 billion spent on the war, at least $160 billion has likely ended up in the coffers of private contractors." Lawsuits are still pending in some cases.[38]

The stakeholder management approach involves the full range of dispute resolution techniques, although ideally more *integrative* and *relational* rather than *distributive* or *power-based* methods would be attempted first. (Power-based approaches are based on authoritarian and competition-based methods where the more powerful group or individual "wins" and the opposing group "loses." This approach can cause other disputes to arise.) Integrative approaches are characterized as follows:

- Problems are seen as having more potential solutions than are immediately obvious.
- Resources are seen as expandable; the goal is to "expand the pie" before dividing it.
- Parties attempting to create more potential solutions and processes are thus said to be "value creating."
- Parties attempt to accommodate as many interests of each of the parties as possible.
- The so-called win–win or "all gain" approach.[39]

Distributive approaches have the following characteristics:

- Problems are seen as zero sum.
- Resources are imagined as fixed: "divide the pie."

- They are "value claiming" rather than "value creating."
- They involve haggling or "splitting the difference."[40]

Relational approaches (which consider power, interests, rights, and ethics) include and are based on:

- Relationship building.
- Narrative, deliberative, and other "dialogical" (i.e., dialogue-based) approaches to negotiation and mediation.
- Restorative justice and reconciliation (i.e., approaches that respect the dignity of every person, build understanding, and provide opportunities for victims to obtain restoration and for offenders to take responsibility for their actions).
- Other transformative approaches to peacebuilding.[41]

The process of principled negotiation from Roger Fisher and William Ury's book, *Getting to Yes*, continues to be used for almost any type of dispute. Their four principles are:

1. Separate the people from the problem.
2. Focus on interests rather than positions.
3. Generate a variety of options before settling on an agreement.
4. Insist that the agreement be based on objective criteria.[42]

Adjudicative, legislative, restorative justice, reparation, and rights-based approaches are necessary when rights, property, or other legitimate claims have been violated and harm results. Leaders and professionals practicing a stakeholder management approach incorporate and gain proficiency in using a wide range of conflict and alternative dispute resolution methods.[43]

3.5 Stakeholder Management Approach: Using Ethical Principles and Reasoning

Applying ethical principles and reasoning in a stakeholder approach involves asking: What is equitable, just, fair, and good for those who affect and are affected by business decisions? Who are the weaker stakeholders in terms of power and influence? Who can, who will, and who should help weaker stakeholders make their voices heard and encourage their participation in the decision process? This approach also requires the principal stakeholders to define and fulfill their ethical obligations to the affected constituencies.

Chapter 2 specifically deals with the ethical principals and reasoning used in a stakeholder approach. That chapter presents several ethical frameworks and principles, including the following: (1) the common good principle, (2) rights, (3) justice, (4) utilitarianism, (5) relativism, and (6) universalism, all of which can be applied to individual, group, and organizational belief systems, policies, and motives. You may also refer to Chapters 2 and 3 when using ethical

principles (or the lack of such) to describe actual individuals' and groups' observed moral policies, motives, and outcomes in cases that you are studying or creating from your experience or research.

3.6 Moral Responsibilities of Cross-Functional Area Professionals

One goal of a stakeholder analysis is to encourage and prepare organizational managers to articulate their own moral responsibilities, as well as the responsibilities of their company and their profession, toward their different constituencies. Stakeholder analysis focuses the enterprise's attention and moral decision-making process on external events. The stakeholder management approach also applies internally, especially to individual managers in traditional functional areas. These managers can be seen as conduits through which other external stakeholders are influenced.

Because our concern is managing moral responsibility in organizational stakeholder relationships, this section briefly outlines some of the responsibilities of selected functional area managers. With the Internet, the transparency of all organizational actors and internal stakeholders increases the risk and stakes of unethical practices. Chat rooms, message boards, and breaking-news sites provide instant platforms for exposing both rumor and accurate news about companies. (In the tobacco controversy, it was an antismoking researcher and advocate who first posted inside information from a whistle-blower on the Internet. This action was the first step toward opening the tobacco companies' internal documents to public scrutiny and the resulting lawsuits.)

Figure 3.7 illustrates a manager's stakeholders. The particular functional area you are interested in can be kept in mind while you read the descriptions discussed next. Note that steps 1 through 7 presented in the stakeholder analysis can also be used for this level of analysis.

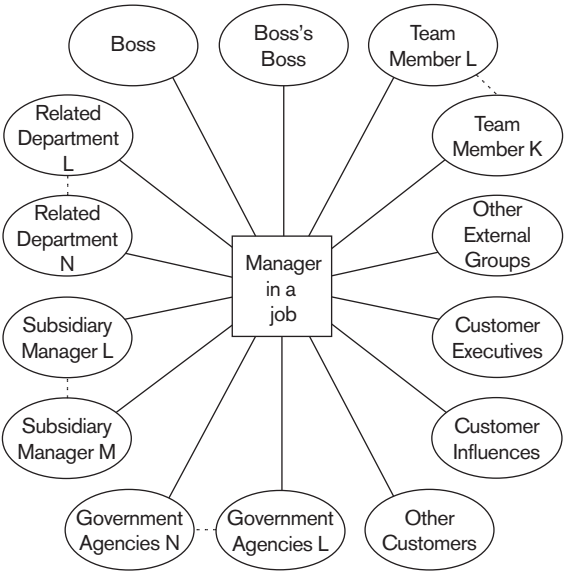
Functional and expert areas include marketing, research and development (R&D), manufacturing, public relations (PR), human resource management, and accounting and finance. The basic moral dimensions of each of these are discussed below. Even though functional areas are often blurred in some emerging network organizational structures and self-designed teams, many of the responsibilities of these managerial areas remain intact. Understanding these managerial roles from a stakeholder perspective helps to clarify the pressures and moral responsibilities of these job positions. Refer to the section on ethical principles and quick ethical tests for professionals in Chapter 2.

Marketing and Sales Professionals and Managers as Stakeholders

Sales professionals and managers are continuously engaged—electronically and/or face-to-face—with customers, suppliers, and vendors. Sales professionals are also evaluated by quotas and quantitative expectations on a weekly,

Figure 3.7

A Manager's Stakeholders



Note: The letters K, L, M, and N are hypothetical designations in place of real department names. Dotted lines refer to hypothetical linkages.

Source: Freeman, R. Edward. (1984). *Strategic management: A stakeholder approach,* 218. Boston: Pitman. Reproduced with permission of the author.

monthly, and quarterly basis. The stress and pressure to meet expectations is always present. Sales professionals must continually balance their personal ethics and their professional pressures. The dilemma often becomes: "Who do I represent? What weight do my beliefs and ethics have when measured against my department's and company's performance measures for me?" Another key question for sales professionals particularly is: "Where is the line between unethical and ethical practices for me?" Also, because customers are an integral part of business, these professionals must create and maintain customer interest and loyalty. They must be concerned with consumer safety and welfare, while increasing revenue and obtaining new accounts. Many marketing and sales professionals also are responsible for determining and managing the firm's advertising and the truthfulness (and legality) of the data and information they issue to the public about products and services. They must interact with many of the other functional areas and with advertising agencies, customers, and consumer groups. Moral dilemmas can arise for marketing managers who may be asked to promote unsafe products or to implement advertising campaigns that are untrue or not in the consumer's best interests.

Several equity traders, particularly at Enron during and after the corporate scandals, were involved in lying to customers about "dogs"—stocks they knew were underperforming. Part of their motive was to keep certain stocks

popular and in a "buy" mode, so their own sales performance would be valued higher, giving them better bonuses.

A major moral dilemma for marketing managers is having to choose between a profitable decision and a socially responsible one. Stakeholder analysis helps marketing managers in these morally questionable situations by identifying stakeholders and understanding the effects and consequences of profits and services on them. Balancing company profitability with human rights and interests is a moral responsibility of marketers. Companies that have no ethics code or socially responsible policies—as well as those that do have these, but do not enforce them—increase the personal pressure, pain, and liability of individual professionals. Such tensions can lead to unethical and illegal activities.

R&D, Engineering Professionals, and Managers as Stakeholders

R&D managers and engineers are responsible for the safety and reliability of product design. Faulty products can mean public outcry, which can result in unwanted media exposure and possibly (perhaps justifiably) lawsuits. R&D managers must work and communicate effectively and conscientiously with professionals in manufacturing, marketing, and information systems, and with senior managers, contractors, and government representatives, to name a few of their stakeholders. This chapter's opening case illustrates that a company's operating parts, design, and quality control can involve more care and concern for safety and monitoring to ensure proper functioning of operations than BP's company officers probably envisioned before that crisis erupted. Technical issues can quickly escalate to political, cultural, legislative, and judicial levels; ethical issues that may begin as professional ethical codes of engineers can, if a product crisis occurs, transform into legal concerns about international human and consumer rights and justice.

As studies and reports on the Space Shuttle *Challenger* disaster that occurred on January 28, 1986, further illustrate, care and attention to the safe functioning of technical parts and processes of any system can mean the difference between life and death. *Challenger* tore apart 73 seconds after lift-off from Cape Canaveral, Florida. Engineers and managers at the National Aeronautics and Space Administration (NASA) and the cooperating company, Thiokol, had different priorities, perceptions, and technical judgments regarding the "go, no-go" decision of that space launch. A follow-up study found that "The commission not only found fault with a failed sealant ring but also with the officials at the National Aeronautics and Space Administration (NASA) who allowed the shuttle launch to take place despite concerns voiced by NASA engineers regarding the safety of the launch."[44] Lack of individual responsibility and the poor critical judgment of NASA administrators contributed to the miscommunication and resulting disaster.

Moral dilemmas can arise for R&D engineers whose technical judgments and risk assessments conflict with administrative managers seeking profit and time-to-market deadlines. R&D managers also can benefit from doing a stakeholder analysis, before disasters like the *Challenger* occur. The discussion

of the levels of business ethics in Chapter 1 also provides professionals with a way of examining their individual ethics and moral responsibilities.

Accounting and Finance Professionals and Managers as Stakeholders

Accounting and finance professionals are responsible for the welfare of clients and safeguard their financial interests. Financial planners, brokers, accountants, mutual fund managers, bankers, valuation specialists, and insurance agents have the responsibility of ensuring reliable and accurate transactions and reporting of other people's money and assets.[45] Many of these professions are part of regulated industries; however, the recent corporate scandals at Enron, Tyco, Arthur Andersen, and other large firms showed that company culture, individual and team judgment, greed, and lack of integrity contributed to executives' "cooking the books." Financial fraud, stealing, and gambling away employees' pensions, and shareholders' investments were part of the illegal activities officers of these firms directed and led. Although the Sarbanes-Oxley Act, the Revised Sentencing Guidelines, and stricter company ethics and reporting codes (see Chapter 4) have helped prevent illegal activity in these professions, problems remain.

Factors in these professions that trigger unethical activities include: (1) pressures from senior officers and supervisors to "maximize profits," sometimes at any cost; (2) lack of integrity (truthfulness, conscience) of leaders, supervisors, and employees; (3) corporate cultures that devalue clients, investors, and employees; (4) requests from clients to change financial statements and tax returns and commit tax fraud; (5) conflict of interest and lack of auditor independence between client and auditing firm; and (6) blurring professional and personal roles and responsibilities between client and professional. These issues are in part related to societal, structural problems. For example, the U.S. financial system emphasizes and rewards short-term, quarterly earnings that help create many of the pressures and poor practices listed above. Chapters 4 and 5 deal with these topics in more detail.

Public Relations Managers as Stakeholders

PR managers must constantly interact with outside groups and corporate executives, especially in an age when communications media, external relations, and public scrutiny play such vital roles. PR managers are responsible for transmitting, receiving, and interpreting information about employees, products, services, and the company. A firm's public credibility, image, and reputation depend on how PR professionals manage stakeholders because PR personnel must often negotiate the boundaries between corporate loyalty and credibility with external groups. These groups often use different criteria than corporate executives do for measuring success and responsibility, especially during crises. Moral dilemmas can arise when PR managers must defend company actions that have possible or known harmful effects on the public or stakeholders. A stakeholder analysis can prepare PR managers

and inform them about the situation, the stakes, and the strategies they must address.

Human Resource Managers as Stakeholders

Human resource managers (HRMs) are on the front line of helping other managers recruit, hire, fire, promote, evaluate, reward, discipline, transfer, and counsel employees. They negotiate union settlements and assist the government with enforcing Equal Employment Opportunity Commission (EEOC) standards. HRMs must translate employee rights and laws into practice. They also research, write, and maintain company policies on employee affairs. They face constant ethical pressures and uncertainties over issues about invasion of privacy and violations of employees' rights. Stakeholders of HRMs include employees, other managers and bosses, unions, community groups, government officials, lobbyists, and competitors.

Moral dilemmas can arise for these managers when affirmative action policies are threatened in favor of corporate decisions to hide biases or protect profits. HRMs also straddle the fine line between the individual rights of employees and corporate self-interests, especially when reductions in force (RIFs) and other hiring or firing decisions are involved. As industries restructure, merge, downsize, outsource, and expand internationally, HRMs' work becomes even more complicated.

Summary of Managerial Moral Responsibilities

Expert and functional area managers are confronted with balancing operational profit goals with corporate moral obligations toward stakeholders. These pressures are considered "part of the job." Unfortunately, clear corporate directions for resolving dilemmas that involve conflicts between individuals' rights and corporate economic interests generally are not available. Using a stakeholder analysis is "like walking in the shoes of another professional": you get a sense of his or her pressures. Using a stakeholder analysis is a step toward clarifying the issues involved in resolving ethical dilemmas. Chapter 2 presented moral decision-making principles that can help individuals think through these issues and take responsible action.

3.7 Issues Management, Integrating a Stakeholder Framework

Issues management methods complement the stakeholder management approach. It may be helpful to begin by identifying and analyzing major issues before doing a stakeholder analysis. Many reputable large companies use issues managers and methods for identifying, tracking, and responding to trends that offer potential opportunities as well as threats to companies.[46] Before discussing ways of integrating stakeholder management (and analysis) with issues management, issues management is defined.

What Is an Issue?

An issue is a problem, contention, or argument that concerns both an organization and one or more of its stakeholders and/or stockholders. Teresa Yancey Crane, founder of the Issue Management Council, explains the relationship between an issue and issue management the following way: "Think of an issue as a gap between your actions and stakeholder expectations. Second, think of issue management as the process used to close that gap."[47] The gap can be closed in a number of ways, using several strategies. A primary method is using an accommodating policy. Providing public education, community dialogue, and changing expectations through communication are some accommodating strategies used in issues management. Solving complicated issues may sometimes require radical actions, like replacing members from the board of directors and the senior management team.[48]

Issues management is also a formal process used to anticipate and take appropriate action to respond to emerging trends, concerns, or issues that can affect an organization and its stakeholders. "Issues management is a . . . genuine and ethical long-term commitment by the organization to a two-way, inclusive standard of corporate responsibility toward stakeholders. Issues management involves connectivity with, rather than control of, others. Issues managers help identify and close gaps between expectation, performance, communication, and accountability. Issues management blends 'many faces' within the entity into 'one voice.' Like the issues themselves, the process is multi-faceted and is enhanced by the strategic facilitation and integration of diverse viewpoints and skills."[49]

Many national and international business-related controversies develop around the exposure of a single issue that evolves into more serious and costly issues. Enron's problems in the beginning surfaced as an issue of overstated revenue. After months of investigation, members of the highest executive team were found to have been involved in deception, fraud, and theft. Ford had the Bridgestone/Firestone Explorer tire crisis in 2001 with what appeared to be faulty tires (see Ethical Insight 3.1). The issue escalated to questions about the design of the Ford vehicle itself, then to questions about many international deaths and accidents over a number of years. The CEO of Ford eventually lost his job.

Ethical Insight 3.1

Classic Crisis Management Case

- Crisis management experts criticized Bridgestone/Firestone for minimizing their tires' problems during the week of August 11, 2000. The experts gave the company mixed reviews on its handling of the recall of 6.5 million tires that were responsible for 174 deaths and more than 300 incidents involving tires that allegedly shredded on the highway in 1999. The tire maker's spokespersons claimed the poor tread on the tires was caused by underinflation, improper maintenance, and poor road conditions.

- Mark Braverman, principal of CMG Associates, a crisis management firm in Newton, Massachusetts, noted that the company blamed the victim and that Bridgestone/Firestone lacked a visible leader for its crisis management effort. "The CEO should be out there, not executive vice presidents."
- Steven Fink, another crisis management expert, noted that "After they [Bridgestone/Firestone] announced the recall, they were not prepared to deal with it. They were telling consumers they will have to wait up to a year to get tires. And things like busy telephone call lines and overloaded web sites—these are things that can be anticipated. That's basic crisis management."
- Stephen Greyser, professor of marketing and communications at Harvard Business School, stated, "It's about what they didn't do up to now. The fact that [Bridgestone/Firestone] is just stepping up to bat tells me they've never really had the consumer as the principal focus of their thinking."
- Defending the way Bridgestone/Firestone handled the crisis was Dennis Gioia, professor of organizational behavior at Smeal College of Business Administration at Pennsylvania State University: "With hindsight, you can always accuse a company of being too slow, given the history of automotive recalls. Sometimes you can't take hasty action or you would be acting on every hint there's a problem. It can create hysteria."

Question for Discussion

Who do you agree or disagree with among these crisis management consultants? Explain.

Source: Consultants split on Bridgestone's crisis management. (August 11, 2000). *Wall Street Journal,* A6.

Other Types of Issues

There are other types of issues arising from the external environment that involve different companies and industries. For example, the issue of obesity has become prominent in the United States. Once considered a personal lifestyle problem, obesity is now seen as a public health disease, and its treatment can be paid for by one's health insurance. This issue involves insurance companies, the corporations who employ individuals facing this problem, employment attorneys, families of those individuals affected, and taxpayers, to name a few. Another issue that affects numerous stakeholders is drivers who drink. U.S. mothers who have lost their children to this growing phenomenon have discovered that this issue is not a set of isolated events, but widespread. Mothers Against Drunk Driving (MADD) was founded in the 1980s by Candy Lightner, whose 13-year-old daughter Cari was killed by a drunken hit-and-run driver as she walked down a suburban street in California. The impact broke almost every bone in her body and fractured her skull, and she died at the scene of the accident. "I promised myself on the day of Cari's death that I would fight to make this needless homicide count for something positive in the years ahead," her mother later wrote.[50]

Programs like *60 Minutes, Dateline,* and *Frontline* introduce breaking news that focuses on events, crises, and innovative practices that are being faced and addressed. Stakeholder and issues management frameworks can be used to understand the evolution of these issues in order to responsibly manage or change their effects.

Stakeholder and Issues Management: "Connecting the Dots"

Issues and stakeholder management are used interchangeably by scholars and corporate practitioners, as the two following quotes illustrate:

> For many societal predicaments, stakeholders and issues represent two complementary sides of the same coin.[51]
>
> Stakeholders tend to organize around "hot" issues, and issues are typically associated with certain vocal stakeholder groups. Issues management scholars can therefore explore how issues management requires stakeholder prioritization, and how stakeholder management gets facilitated when managers have deep knowledge of stakeholders' issue agendas. Earlier research also suggests that whether or not stakeholders decide to get involved with certain issues has a profound influence on issue evolution, and as does the timing and extent of their involvement.[52]

Applying stakeholder and issues management approaches should not be mechanical. Moral creativity and objectivity help, as discussed in Chapter 1. A general first step is to ask: "What is the issue, opportunity, or precipitating event that an organization is facing or has experienced? How did the issue emerge?" Generally there are several issues that are discovered. The process begins by analyzing and then framing which issues are the most urgent and have (or may have) the greatest impact on the organization. At this point, you can begin to ask who was involved in starting or addressing the issue. This triggers the beginning of a stakeholder analysis and the steps discussed earlier in the chapter. Depending on how the issue evolved into other issues—or whether there was a crisis at the beginning, middle, or end of the issue evolution—you will know which issues management framework from the following section is most relevant for the analysis of the situation.

Actually, stakeholder analysis questions help "connect the dots" in understanding and closing the gaps of issues management. Stakeholder questions help discover "who did what to whom to influence which results, and at what costs and outcomes." A major purpose in analyzing and effectively managing issues and stakeholders is to create environments that enable high-performing people to achieve productive and ethical results.

Moral Dimensions of Stakeholder and Issues Management

Some studies argue that moral reasoning is "issue-dependent" and that "people generally behave better when the moral issue is important."[53] Questions regarding issue recognition include: To what extent do people actually recognize moral issues? Is it by the magnitude of the potential consequences or the

actual consequences of the issue? Is it by the social consensus regarding how important the issue is? Is it by how likely it is that the effects of the issue will be felt or how quickly the issue will occur?[54] Ethical reasoning and behavior are an important part of managing stakeholders and issues because ethics is the energy that motivates people to respond to issues. When ethical motives are absent from leaders' and professionals' thinking and feeling, activities can occur that cost all stakeholders. Teaching you to detect and prevent unethical and illegal actions by using these methods is an aim of this section.

Companies face issues every day. Some issues lead to serious consequences—defective products, financial fraud, fatal side effects of drugs, oil spills, the loss of millions of lives to the effects of tobacco, violence from use of firearms, or the theft of pensions from ordinary employees who worked a lifetime to accrue them. Other issues evolve in a way that leads to spectacular outcomes: the invention and commercialization of the Internet, information technology that provides wireless access to anyone at any time in any place, and the capability to network customers, businesses, suppliers, and vendors. Learning to identify and change issues for the good of the organization and for the common and public good is another goal of the stakeholder management approach.

Types of Issues Management Frameworks

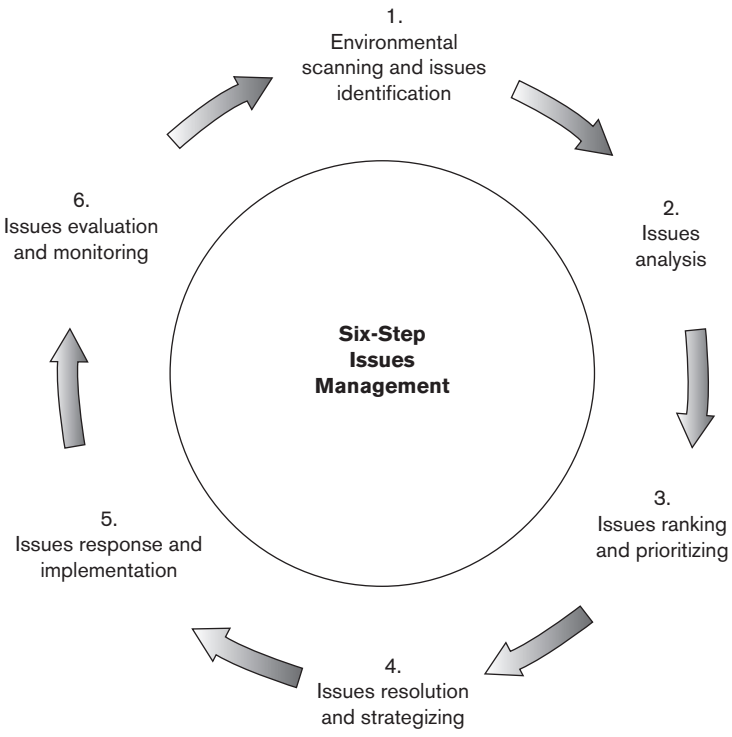
This section presents two general issues frameworks for mapping and managing issues before and after they evolve or erupt into crises. These frameworks can be used with the stakeholder management approach. Using a stakeholder analysis (which is part of the general stakeholder management approach) explains the "who, what, where, why, and what happened" that affects an issue. After you have read the first two issues management approaches shown in Figures 3.8 and 3.9, you will see that either or both can be used to identify and analyze a major issue (crisis or potential opportunity) for an organization, as is explained below.

Figure 3.8 illustrates a straightforward framework that organizations can use for anticipating and thinking through issues to prevent a crisis. This is a somewhat generic model that has evolved within the issues management field. Identifying, tracking, and developing responses to issues are the thrusts of the process. More recently, companies like General Electric, Patagonia, Costco, and others use issues frameworks with the intent of acting in socially responsible ways, not only to protect their own companies and businesses from environmental and economic "threats," but also to protect the environment and extend their reputations for "doing the right thing."

The steps in Figure 3.8, then, can also be used to plan and manage issues that may have already affected an organization. Senior officers and staff would probably use this framework in their strategizing and "what if" scenarios. If you are analyzing a case such as the BP rig explosion and oil spill, you can use this framework to show what steps the organization *could* have taken to prevent such disasters, and the steps actually taken to manage the issues under

Figure 3.8

Six-Step Issues Management Process



Source: Based on Coates, J., Jarratt, V., and Heinz, L. (1986). *Issues management.* Mt. Airy, MI: Lomond Publications, 19–20.

investigation. You can also use a stakeholder analysis at any point in this model.

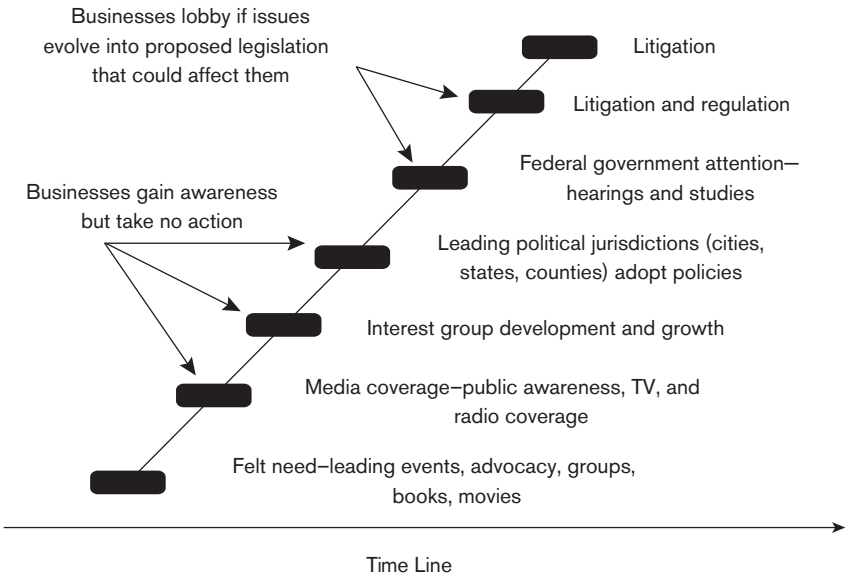
Figure 3.9 is more specific and focuses on the evolution of an issue from inception to resolution. This framework, which is not organization-specific like Figure 3.8, is more likely to be used by analysts, managers, and scholars studying issues that have warning signs which, if attention is given to them, can prevent escalating problems. In many cases, a stakeholder analysis can show why strategies and actions of particular stakeholders short-circuited the issue's evolution through all the stages in this figure.

First Approach: Six-Step Issues Management Process

The first method, as noted, is the most straightforward and most appropriate for companies or groups scanning the environment for issues that can impact their businesses and internal environments. A third-party observer could also use this approach to describe how a company acted in retrospect or could act in the future.

Figure 3.9

Seven-Phase Issue-Development Process



Source: Adapted on Marx, T. (1986). Integrating public affairs and strategic planning. *California Management Review, Fall, 29(1),* 145.

However, this model would not be suitable for examining how an issue evolved over time, or for analyzing precrisis signs or symptoms of an event.

The process involves the following steps, illustrated in Figure 3.8.[55]

1. Environmental scanning and issues identification.
2. Issues analysis.
3. Issues ranking and prioritizing.
4. Issues resolution and strategizing.
5. Issues response and implementation.
6. Issues evaluation and monitoring.

These steps are part of a firm's corporate planning process. In the strategic issues management process, a firm uses a selected team to work on emerging trends as they relate to the industry and company. As Heath noted, "The objective of issues management is to make a smart, proactive, and even more respected organization. This sort of organization is one that understands and responds to its stakeseekers and stakeholders."[56]

This framework is a basic approach for proactively mapping, strategizing, and responding to issues that affect an organization. With regard to this chapter's opening case, if you, as an objective third-party observer, were analyzing BP's situation, what issues can you identify that might affect the company? As you identify each issue (step 1), you might begin to analyze any

organizational and/or environmental issue that offered clues about the condition of the rig. Then you could examine the issues and their impact on the organization and other stakeholders before and after the explosion (step 2). The remaining steps would involve analyzing how BP handled the crisis (steps 3–6).

This six-step process also enables you to advise upper-level managers and directors in the company regarding precautions to take to avoid the illegal and unethical consequences of an issue. This model sharpens your ability to see the effects of issues on organizations from conception to response and monitoring.

Second Approach: Seven-Phase Issue Development Process

Issues are believed and have been observed to follow a developmental life cycle. Views differ on the stages, phases, and time involved in such a life cycle. Thomas Marx's reasoning fits with the seven-phase evolution of a public's "felt need" or outcry through that need or demand's becoming a law. The entire cycle has been estimated at taking eight years, as illustrated in Figure 3.9—with the use of the Internet, social media, and mobile devices, this time span will likely be shortened.[57]

1. A felt need arises (from emerging events, advocacy groups, books, movies).
2. Media coverage is developed (television segments, such as on *60 Minutes, 20/20, FOX News, CNN,* and breaking news on the Internet from the *Wall Street Journal, New York Times,* and other news and blogging sources).
3. Interest group development gains momentum and grows.
4. Policies are adopted by leading political jurisdictions (cities, states, counties).
5. The federal government gives attention to the issue (hearings and studies).
6. Issues and policies evolve into legislation and regulation.
7. Issues and policies enter litigation.

BP's CEO and top-level team could have used this framework to anticipate and perhaps prevent the explosion; and if not prevent the explosion, they could have responded to the public in a more timely and concerned way. With the Internet, it no longer takes seven years for this model to move from phase one to the last (litigation) phase. Once local and federal legislators learn about a volatile news-breaking public issue, especially if the media has exposed it, company representatives may respond sooner.

"While the accident could have been prevented, BP might have avoided its intense and deserved public flogging if only it had respected the best practices for managing a crisis."[58] Bryant and Hunter go on to explore who is to blame for the spill:

> BP has for many years publicly claimed to be laser focused on safety. But inside the company, it was clearly focused on cost cutting, at the expense of safety. Furthermore, regulators and environmental groups have not been fooled by BP's public statements, though they have allowed the company to continue to

operate as usual. Who then is to blame for the spill? Is it BP, which has been driving cost cutting hard and succeeding? Or its contractors, who have had to operate to meet BP's specifications and who, in order to meet budget, changed operating procedures? Is it government regulators, who have been well aware of BP's violations, but have allowed it not to pay its fines and to continue to operate? Is it the public, users of oil, whose insatiable demands for petrochemical products has led to the overuse of a limited natural resource that, it could be claimed, forced firms like BP to take on ever more risky operations to meet demand (note that figures suggest that the operations in the Gulf account for nearly 20 percent of the United States' domestic oil production)? Or, is it investors, demanding ever higher returns on their investment over shorter periods of time, driving BP executives to squeeze efficiencies from operations that were designed to be effective—not efficient, in order to maximize earnings per share?[59]

Stakeholder management methods can be used with this issue management approach in order to identify those groups and individuals who moved an issue from one phase to another and who helped change the nature of an issue. Usually different stakeholder groups redefine issues as these constituencies compete with one another, using different sources of power, as discussed earlier.

This seven-phase framework is also useful in identifying and following public issues that do not necessarily originate with corporations, and could be applied to such issues as drunk-driving, obesity, global warming, and even to natural disasters such as Hurricane Sandy in 2012, Katrina in 2005, or the 2004 Indian Ocean earthquake and tsunami. Issues frameworks and stakeholder analysis can help identify the effectiveness of public and private organizations in detecting and responding to events that result in crises. Sometimes the aftermath of a catastrophic event can result in a larger crisis than the precipitating event itself.

Marx illustrated his model with the origins of the automobile safety belt issue.[60] The four stages of this case, according to Marx, were reflected by the following events:

1. Social awareness: Ralph Nader's now-classic book, *Unsafe at Any Speed,* published in 1965, created a social expectation regarding the safe manufacturing of automobiles. The Chevrolet Corvair, later pulled off the market, was the focus of Nader's astute legal and public advocacy work in exposing manufacturing defects.
2. Political awareness: The National Traffic and Motor Vehicle Safety Act and the resulting safety hearings in 1966 moved this expectation into the political arena.
3. Legislative engagement: In 1966, the Motor Vehicle Safety Act was passed, and four states began requiring the use of seat belts in 1984.
4. Litigation: Social control was established in 1967, when all cars were required to have seat belts. Driver fines and penalties, recalls of products, and litigation concerning defective equipment further reinforced the control stage.

Nader's pioneering consumer advocacy and legal work with regard to U.S. automobile manufacturing set an enduring precedent for watchdog congressional and voluntary advocacy groups that initiated laws that are still in effect.

Many other books have served as catalysts to mobilize the U.S. public and ultimately influence Congress to pass legislation. A brief list includes, for example, Thomas Paine's *Common Sense* (1776), which rallied the public against the British monarchy and is believed to have been the single most powerful influence that mobilized widespread support for the Revolutionary War—over 100,000 copies were sold in the first few months of its publication. Mary Wollstonecraft's *A Vindication of the Rights of Women* (1792) was the first literary statement promoting women's rights and led to the movement that gave women the right to vote in America. Upton Sinclair's novel *The Jungle* (1906) shocked the nation by exposing the wretched conditions of Chicago's meatpacking industry and the impoverished lives of immigrants who worked there. The book influenced legislation on employment laws and safety standards related to meatpacking and the food industry in general. *Silent Spring* (1962) by Rachel Carson brought to the attention of millions the loss of endangered species and the environment and pressured some of the first legislation in these areas.[61] Refer to Chapter 5 to see later books on food and diets that also have made an impact on national policy.

Take any industry or scan the news, then select an issue and see if you can predict and/or observe the possible path the issue may take through these different stages. This issue evolution process provides a window into the emergence and evolution of public policies and laws in U.S. society. Issues are not static or predetermined commodities. Stakeholder interests and actions move or impede an issue's development. To understand how an issue develops, or is unable to develop, is to understand how power works in a political system in which market and nonmarket forces pressure the ethics and values of stockholders and stakeholders.

3.8 Managing Crises

On January 15, 2009, US Airways Flight 1549 took off from LaGuardia Airport in New York City bound for Charlotte/Douglas International Airport, North Carolina, with the ultimate destination of Seattle-Tacoma International Airport in Washington. During its initial climb, the plane hit a flock of Canadian Geese. Despite losing engine power, Captain Chesley Burnett "Sully" Sullenberger III and his crew safely landed the plane on the Hudson River off midtown Manhattan. That landing is now known as the "Miracle on the Hudson." The crew was later awarded the Master's Medal of the Guild of Air Pilots and Air Navigators, which stated "This emergency ditching and evacuation, with the loss of no lives, is a heroic and unique aviation achievement." It was later described as "the most successful ditching in aviation history."[62]

Captain Sullenberger's crisis leadership style was focused, technically and intuitively accurate and creative, calm, sympathetic, positive, and transparent.

Consequently, his leadership during a time of intense crisis is celebrated as heroic, although he personally does not feel comfortable with that term. Captain Sullenberger's actions that day now serve as an exemplary role model of crisis leadership.[63]

Crisis management methods evolved from the study of how corporations and leaders responded (and should have responded) to crises. Using crisis management methods with stakeholder management methods is essential for understanding and possibly preventing future fiascos because crises continue to occur in a number of areas: product/service crises (e.g., JetBlue's 2007 weather-related mishap); consumer products (the classic crisis with Ford's use of faulty Bridgestone/Firestone tires), financial systems (Enron and the recent subprime lending crisis), and government/private contractor projects (Boston's 2006 Big Dig tunnel partial ceiling collapse and the 1986 *Challenger* disaster). Captain Sullenberger's response to the crisis he faced in the scenario discussed above is a success story. Unfortunately, most corporate leaders have not responded so courageously.

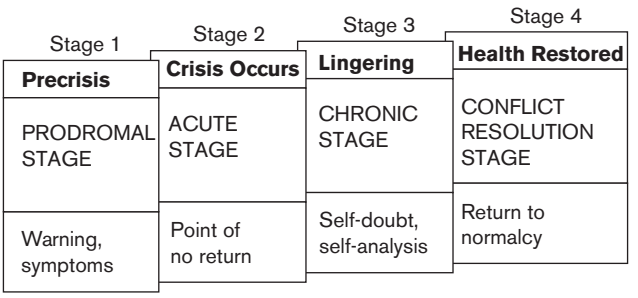
Steven Fink states that a crisis is a "turning point for better or worse," a "decisive moment" or "crucial time," or "a situation that has reached a critical phase." He goes on to say that crisis management "is the art of removing much of the risk and uncertainty to allow you to achieve more control over your destiny."[64] Crises, from a corporation's point of view, can deteriorate if the situation escalates in intensity, comes under closer governmental scrutiny, interferes with normal operations, jeopardizes the positive image of the company or its officers, or damages a firm's bottom line. A turn for the worse also could occur if any of the firm's stakeholders were seriously harmed or if the environment was damaged. The following two approaches describe ways that organizations can respond to crises. You may turn to Chapter 4 to review some of the classic corporate crises, in addition to the more contemporary BP rig explosion and oil spill, that have occurred over the past few decades. Having such examples as the *Exxon Valdez,* the Ford Pinto disaster, and other crises in mind would be informative as you read how to examine and respond to a crisis from a stakeholder management perspective.

The model in Figure 3.10 shows a crisis consisting of four stages: (1) prodromal (precrisis), (2) acute, (3) chronic, and (4) conflict resolution. Judgment and observation are required to manage these stages. This approach differs from the second one in that a precrisis stage is included.[65]

The *prodromal* stage is the warning stage. If this stage is not recognized or does not actually occur, the second stage (acute crisis) can rush in, requiring damage control. Clues in the prodromal stage must be carefully observed. For example, BP blamed Transocean and Halliburton for the explosion; these companies blamed BP for taking a laissez-faire or lax approach to safety and equipment that required upgrading. What happens in the prodromal stage when these types of attitudes and values clash within and between companies and work groups? Was there a warning sign or symptom that employees and managers at BP and/or the licensed companies saw that a crisis was possible? If so, why do you think these warning signs were not taken more seriously?

Figure 3.10

Four Crisis-Management Stages



Fink, S. (1986). Crisis management: Planning for the inevitable. New York: American Management Association, 26.

In the second stage, *acute crisis,* damage has been done. The point here is to control as much of the damage as possible. This is often the shortest of the stages. In the BP crisis, the explosion took the crew on the rig by surprise. Should they have been more suspecting that a crisis or problem like this could occur?

The third stage, *chronic crisis,* is the clean-up phase. This is a period of recovery, self-analysis, self-doubt, and healing. Congressional investigations, audits, and interviews occur during this stage, which can linger indefinitely, according to Fink. A survey of Fortune 500 CEOs reported that companies that did not have a crisis management plan stayed in this stage two and a half times longer than those who did. Did BP's leaders' actions during the chronic stage of the crisis change from the way they reacted during the first stage? Why or why not?

The final stage, *crisis resolution,* is the crisis management goal. The key questions here are: What can and should an organization's leaders do to speed up this phase and resolve a crisis once and for all? Has BP learned from the disaster? Are new safety issues and requirements in effect at present?

How Executives Have Responded to Crises

Not all CEOs and organizational leaders respond the same to crises. JetBlue's founder and CEO, David Neeleman (who is still revered in the company), resigned as CEO and issued a customer "Bill of Rights" after one of the worst crisis in the airline's history during the winter of 2007, when "nine airplanes full of angry passengers sat for six hours or more on the tarmac at John F. Kennedy International Airport in New York,"[66] costing the airline $30 million. A classic crisis management model developed by Archie Carroll suggests a different type of CEO response mode in its five phases of corporate social response to crises related to product crises.[67] This model illustrates how corporations have, and many continue to, actually responded to serious crises. The phases, illustrated in Figure 3.11, are (1) Reaction, (2) Defense, (3) Insight,

Figure 3.11

Corporate Social Responses

Source: Adapted from Carroll, A. (1977). A three-dimensional conceptual model of corporate performance. *Academy of Management Review, 4(4),* 502.

(4) Accommodation, and (5) Agency. For a full description of the BP crisis, a more thorough case appears at the end of this chapter and can be used to apply the crisis management methods presented here. Did the then BP CEO react first and then respond? If so, why do you think many CEOs go into a "reaction" mode at the first realization of a crisis?

It is interesting to observe how some executives continue to deny and/or avoid responsibility in crises that become disastrous. Knowledge of these stages certainly would be a first step toward corporate awareness. Let's look more closely at each stage.

According to this model, the *Reaction* stage is the first phase when a crisis has occurred. Management lacks complete information and time to analyze the event thoroughly. A reaction made publicly that responds to allegations is required. This stage is important to corporations, because the public, the media, and the stakeholders involved see for the first time who the firm selects as its spokesperson, how the firm responds, and what the message is. Notice that a classic crisis in which the leadership and management of a company responded positively—and did not react either negatively or with denial—to a crisis was the Tylenol case. In 1982, seven people died after taking Tylenol capsules that had been tampered with and laced with cyanide. Tylenol's market sank from 37% to 7%. James Burke, Johnson & Johnson's chairman, and a seven-member team focused first on protecting people and customers, then saving the product. Thirty-one million bottles of Tylenol nationally were recalled and all advertising was stopped until the problem was solved. An 800 number was set up and corporate headquarters held several press conferences with a live satellite feed. Two months later, "Tylenol was reintroduced into the market with triple-seal tamper-resistant packaging, [and the company] offered coupons for the products, created a new discounted pricing program, new advertising campaign and gave more than 2,250 presentations to the medical community."[68] Two management crises experts said that Johnson & Johnson actually increased their credibility after the crisis, and that their response became the "gold standard" for responding to crises.[69]

The second stage of the model, *Defense,* signals that the company is overwhelmed by public attention. The firm's image is at stake. This stage usually involves the company's recoiling under media pressure. But this does not always have to be a negative or reactive situation.

The third stage, *Insight,* is the most agonizing time for the firm in the controversy. The stakes are substantial. The firm's existence may be questioned. The company must come to grips with the situation under circumstances that have been generated externally. During this stage, the executives realize and confirm from evidence whether their company is at fault in the safety issues of the product in question.

In the fourth stage, *Accommodation,* the company either acts to remove the product from the market or refutes the charges against product safety. Addressing public pressure and anxiety is the task in this stage.

During the last stage, *Agency,* the company attempts to understand the causes of the safety issue and develop an education program for the public.

How could the CEO in the BP case have performed differently according to this model of crisis management? Research news and media reports on the Internet on this and other crises. Take special note of how companies respond morally to their stakeholders. Observe the relative amount of attention companies sometimes give to consumers, the media, and government stakeholders. Use the frameworks presented in this chapter to help inform your observations and judgments. Develop a timeline as the crisis unfolds. Notice who the company chooses as its spokesperson. Determine how and why the company is assuming or avoiding responsibility.

Crisis Management Recommendations

A number of suggestions that corporations can follow to respond more effectively to crises are briefly summarized here. More in-depth strategies and tactics can be found in several sources.[70]

- Face the problem: Don't avoid or minimize it. Tell the truth.
- Take your "lumps" in one big news story rather than in bits and pieces. "No comment" implies guilt.
- Recognize that, in the age of instant news, there is no such thing as a private crisis.
- Stage "war games" to observe how your crisis plan holds up under pressure. Train executives to practice press conferences, and train teams to respond to crises that may affect other functional areas or divisions.
- Use the firm's philosophy, motto, or mission statement to respond to a crisis. For example, "We believe in our customer. Service is our business."
- Use the firm's closeness to customers and end users for early feedback on the crisis and to evaluate your effectiveness in responding to the events.

The following tactical recommendations are also helpful crisis prevention and management techniques:

- Understand your entire business and dependencies.
- Understanding your business provides the basis upon which all subsequent policies and processes are based and, therefore, should not be rushed.

- Carry out a business impact assessment.
- Having identified the mission critical processes, it is important to determine what the impact would be if a crisis happened. This process should assess the quantitative (such as financial and service levels) and the qualitative (such as operational, reputation, legal and regulatory) impacts that might result from a crisis and the minimum level of resource for recovery.
- Complete a 360-degree risk assessment, where managers, their peers and direct reports evaluate each other's style and performance. This is used to determine the internal and external threats that could cause disruption and their likelihood of occurrence. Utilizing recognized risk techniques, a score can be achieved, such as high-medium-low, 1 to 10, or unacceptable/acceptable risk.
- Develop a feasible, relevant, and attractive response. There are two parts to this stage: developing the detailed response to an incident and the formulation of the business crisis plan that supports that response.
- Plan exercising, maintenance, and auditing. A business crisis plan cannot be considered reliable until it has been tested. Exercising the plan is of considerable importance, as a plan untested becomes a plan untrusted.[71]

Finally, issues and crisis management methods and preventive techniques are only effective in corporations if:

- Top management is supportive and participates.
- Involvement is cross-departmental.
- The issues management unit fits with the firm's culture.
- Output, instead of process, is the focus.[72]

Chapter Summary

Organizations and businesses in the twenty-first century are more complex and networked than in any previous historical period. Because of the numerous transactions of corporations, methods are required to understand an organization's moral obligations and relationships to its constituencies.

The stakeholder management approach provides an analytical method for determining how various constituencies affect and are affected by business activities. It also provides a means for assessing the power, legitimacy, and moral responsibility of managers' strategies in terms of how they meet the needs and obligations of stakeholders.

Critics of stakeholder theory argue that corporations should serve only stockholders since they own the corporation. They hold that stakeholder theory: (1) negates and weakens fiduciary duties managers owe to stockholders, (2) weakens the influence and power of stakeholder groups, (3) weakens the firm, and (4) changes the long-term character of the capitalist system. A major response to the critics of stakeholder theory states that societies and economies involve market and nonmarket interests of diverse stakeholders as

well as stockholders. To understand and effect responsible corporate strategies, methods that include different players and environmental factors—not just stockholders or financial interests—are required.

A stakeholder analysis is a strategic management tool that allows firms to manage relationships with constituents in any situation. An individual or group is said to have a "stake" in a corporation if it possesses an interest in the outcome of that corporation. A "stakeholder" is defined as an individual or group who can affect or be affected by the actions or policies of the organization.

Recent studies have indicated that profits and stockholder approval may not be the most important driving forces behind management objectives.[73] Job enrichment, concern for employees, and personal well-being are also important objectives. These studies reinforce the importance of the stakeholder management approach as a motivating part of an organization's social responsibility system.

The implementation of a stakeholder analysis involves a series of steps designed to help a corporation understand the complex factors involved in its obligations toward constituencies.

The moral dimensions of managerial roles also have a stakeholder perspective. The stakeholder approach can assist managers in resolving conflicts over individual rights and corporate objectives. This approach can help managers think through and chart morally responsible decisions in their work.

The use of stakeholder analysis by a third party is a means for understanding social responsibility issues between a firm and its constituencies. Ethical reasoning can also be analyzed relative to the stakeholder management approach.

Preventing and effectively negotiating disputes is a vital part of the work of professionals and leaders. We discussed several alternative dispute resolution (ADR) methods in the chapter, emphasizing consensual, relational, and integrative methods that seek win–win approaches. The full range of dispute resolution methods is important to learn because conflict is part of ongoing organizational change.

Issues and crisis management frameworks complement stakeholder analysis as social responsibility methods. Understanding what the central issues are for a company and how the issues evolved over time can help effectively and responsibly manage changes in a company's direction and operations. Crisis management frameworks help to predict, prevent, and respond to emergencies. Issues and stakeholder management methods used together provide an overall approach to leading and managing organizational change responsibly and ethically.

Questions

1. With regard to this chapter's opening case, what, if anything, could BP's CEO have done differently to have prevented and/or avoided the resulting fall-out from the crisis? Explain.

2. Briefly describe a dispute in which you were an important stakeholder. How was the situation resolved (or not resolved)? What methods were used to resolve the situation? Looking back now, what methods could or should have been used to resolve that situation? For example, what would you now recommend happen to effectively resolve it fairly?
3. Which of the types of power (described in this chapter) that stakeholders can use have you effectively used in a conflict or disagreement over a complex issue? Briefly explain the outcome and evaluate your use(s) of power.
4. Which roles and responsibilities in this chapter have you assumed in an organization? What pressures did you experience in that role that presented ethical dilemmas or issues for you? Explain.
5. What reasons would you offer for encouraging leaders and/or managers to use the stakeholder approach? Would these reasons apply to teams?
6. Give a recent example of a corporation that had to publicly manage a crisis. Did the company spokesperson respond effectively to stakeholders regarding the crisis? What should the company have done differently in its handling of the crisis?
7. Describe how you would feel and what actions you would take if you worked in a company and saw a potential crisis emerging at the prodromal or precrisis stage. What would you say, to whom, and why?
8. Using Figure 3.4, identify a complex issue-related controversy or situation in which you, as a stakeholder, were persuaded to move from one position (cell) to another and why–for example, from Nonsupportive to Supportive, or from Mixed Blessing to Marginal. Explain why you moved and what the outcome was.
9. Argue both the pros and cons of stakeholder theory, using some of the arguments in the chapter as well as your own. What is your evaluation of the usefulness of the stakeholder management approach in understanding and analyzing complex issues?

Exercises

1. Describe a situation in which you were a stakeholder. What was the issue? What were the stakes? Who were the other stakeholders? What was the outcome? Did you have a win–win resolution? If not, who won, who lost, and why?
2. Recall your personal work history. Who were your manager's most important stakeholders? What, in general, were your manager's major stakes in his or her particular position?
3. In your company or organization, or one in which you have worked, what is the industry? The major external environments? Your product or service? Describe the major influences of each environment on your company (for example, on its competitiveness and ability to survive). Evaluate how well your company is managing its environments strategically, operationally, and technologically, as well as in relation to products and public reputation.
4. Choose one type of functional area manager described in the chapter. Describe a dilemma involving this manager, taken from a recent media report.

Discuss how a stakeholder analysis could have helped or would help that manager work effectively with stakeholders.

5. Describe a complex issue that is evolving in the news or media. Explain how the issue has evolved into other issues. Which issues management framework would help track the evolution of this issue? Explain.
6. Describe a recent crisis that involved a product. Which phase of the crisis management model do you believe is the most important for all involved stakeholders? Explain.

Real-Time Ethical Dilemma

I worked as a marketing manager in Belgium for a mid-sized engineering company. Total revenues for the company were $120 million. The company had recently gone public and, in two public offerings, had raised more than $60 million. The firm was organized into four distinct strategic business units, based on products. The group that I worked in was responsible for more than $40 million in sales. We had manufacturing plants in four countries.

Our plant in Belgium manufactured a component that was used in several products, which produced $15 million in revenue. However, these products were old technology and were slowly being replaced in the industry. The overhead associated with the plant in Belgium was hurting the company financially, so they decided to sell the facility. The unions in Belgium are very strong and had not approved the final sale agreement. After this sale, the workforce was going to be reduced by half. Those who were laid off were not going to receive full severance pay, which, in Belgium, could take several years, and then workers would receive only 80% of total payment—a drastic change from what is offered in the United States. I was surprised that our executives in the United States had stated that the sale agreement was more than fair—contrary to the union's position. A strike was imminent; the materials manager was told to stock 10 weeks of product.

My ethical dilemma started after the strike began. Originally, the company thought the strike would not last longer than a couple of days. Instead of causing a panic among our customers, management decided to withhold information on the strike from our customers and sales force. I could understand the delay in telling our customers, but to withhold information from our sales force was, I believed, unconscionable. Inevitably, our inside sales representatives became suspicious when they called the Belgium plant to get the status of an order, and nobody answered. They called me, and I ignored the corporate request and informed them of the strike. When it became obvious that the strike was going to be longer than anticipated, I asked the vice presidents of marketing and sales about our strategy for informing the affected customers. They looked at me quizzically and told me to keep things quiet ("don't open a can of worms") because the strike should be over soon. In addition, they dictated that Customer Service should not inform customers of the strike and excuses should be developed for late shipments.

The strike lasted longer than 12 weeks. In this time, we managed to shut down a production line at Lucent Technologies (a $5-million customer) with only a couple of days notice and alienated countless other valuable and loyal customers. I did not adhere to the company policy: I informed customers about the strike when they inquired about their order status. I also told Customer Service to direct any customer calls to me when we were going to miss shipments. This absolved them of the responsibility to tell the customer.

We did not take a proactive stance until 11 weeks into the strike, when the vice president of sales sent a letter informing our customers about the strike—too little and much too late to be of any help. The materials manager

was fired because he only stocked 10 weeks of product, even though management thought he should have been conservative with his estimates. Halfway through this ordeal, I updated my resume and started a search for a new job. It was clear that management was more concerned about their year-end bonus than doing the right thing for the long-term prospects of the company and its customers.

Questions

1. Do you agree with the writer's decision to inform customers about the strike? Explain.
2. Did management have the right to withhold this information from customers? Explain.
3. Explain what you would have done, and why, if you had been in the writer's situation.
4. What should management have done in this case? When? Why?

Cases

Case 6

The BP *Deepwater Horizon* Explosion and Oil Spill: Crisis and Aftermath

The BP *Deepwater Horizon* spill is a multifaceted disaster that, despite popular opinion, cannot be explained by any one root cause. The April 20, 2010 oil spill was a point of crisis for oil giant BP, and CEO Tony Hayward faced a significant challenge in responding to this crisis.

The events leading up to the BP blowout unearth a highly complex network of circumstances, which though preventable, together culminated in the worst environmental disaster in American history. Repercussions of the incident are still felt today, and all stakeholders involved have an opportunity to learn about the significance of crisis management.

Events Leading up to the BP Spill

In March 2008, the Occupational Safety and Health Administration (OSHA) stated on public record that BP had one of the worst safety records in its industry. This same month, the Minerals Management Service (MMS) gave BP an exclusive right to drill a parcel of Gulf of Mexico floor called Block 252, for a fixed fee of $34 million. Over the coming months, BP boarded a rig to supervise contractors who set out to drill the Macondo well using Transocean rigs.

On October 2009, Hurricane Ida hit the drilling site, damaging BP's oil rig and requiring BP to rent a more technologically sophisticated rig, called *Deepwater Horizon.*

The Point of Crisis

On April 9, 2010, BP exerted unreasonable pressure during drilling and fractured the rock in its well. According to the National Commission on the BP *Deepwater Horizon* Oil Spill and Offshore Drilling, "BP informed its lease partners Anadarko and MOEX that 'well integrity and safety' issues required the rig to stop drilling further." BP management compared safety to profit-maximization and made the decision to plug the fractures in an effort to maximize profit, rather than cease drilling. The plug worked, but BP knew it was precarious, and that they needed to mitigate this risk by balancing pressure carefully. After the incident, BP wells leader admitted that losing returns "was the No. 1 risk."

The Warning Signs

When BP and Halliburton tested float valves, BP used a decision tree to evaluate the job based on whether there were lost returns on the cement factor, rather than engineering or risk principles and decided the test went well enough to excuse Schlumberger technicians, who were also scheduled to perform cement evaluation tests. That decision, which was based on an effort to save the

company time and money, was another example of a decision that could have prevented the oil well blowout that is ironically costing over $20 billion in remediation to date.

BP is documented to have sought Halliburton's counsel on how it could use cement centralizers to mitigate some of this drilling risk. However, due to low inventory, BP again allegedly compromised on quality and safety by changing Halliburton's design and using the wrong kind of cement centralizers.

Halliburton conducted a routine cement slurry test which revealed that the foam was unstable, but they did not adequately report or address it. This event was sadly not uncommon among the various subcontractors on the *Deepwater Horizon* project. There appeared to be a team culture of poor communication driven by an effort to save time, money, and reputation, which ironically resulted in catastrophic loss of the same, at the expense of stakeholders of this project.

The company finished its cement job and began to lock down the Macondo well so it could move a smaller rig into place, but BP had amended *Deepwater's* procedures to omit a pressure test (which would have checked the bottomhole cement job), among other things. (Incidentally, on April 12, BP had sent its amendments to the procedure to the MMS, but there is no evidence that they were reviewed.) While this combination of events, which were caused by several actors, was highly uncanny and improbable, given the circumstances of the weak cement job, their occurrence proved to be deadly. The more that the details of the story were unraveled, the more sweeping the participation among parties and stakeholders in the negligence, insufficient funding, and insufficient communication that led to the *Deepwater Horizon* explosion surfaced.

BP was also discovered to have used a broken pressure gauge during this same time. This too became a critical issue that, if it had been prevented, could have possibly averted the disaster. Still, the root cause of these errors is unclear, as the disaster could have been prevented with tighter risk management protocol, more sufficient inspection, as well as closer attention to fluctuation in gauge readings. Nonetheless, incompetence and risk mitigation planning negligence again appeared to be rife on the job.

Other important precrisis warnings included the fact that the well was leaking and was in danger of exploding. The site workers were also found to have not adequately read or responded to the confounding results of the pressure test, i.e., they needed to use a different gauge to detect a leak that was later found in the well. This also indicated negligence (and incompetence) on behalf of site workers as they should have checked for this. Drill-pipe pressure increased 250 psi as shown on the monitor, but no one appeared to be checking the monitor. As could be expected from these warnings, the pressure relief valve soon blew. In response to this, the pumps were shut off; but pressure increased and no one seemed trained to know the significance of this issue and appropriate action was not taken. The warning signs were ignored.

Next, mud emerged on rig floor indicating that there was a problem in the well. Six–eight minutes passed before this was addressed, and the spill was not diverted overboard. The lack of response indicated negligence in emergency

response training and a disregard for the warning signs that a crisis was coming.

After countless emergency indications, a high enough concentration of natural gas leaked into the air to cause an ignition. This explosion forced five million barrels of oil into the Gulf of Mexico over 87 days; the worst environmental disaster in American history.

The Aftermath—Response to the Crisis

During the emergency response, scientists, including Ian MacDonald of Florida State University, alleged that BP withheld the facts around the spill, likely to protect its reputation. Possibly due to this obfuscation, it took 87 days until the well was finally capped on July 15, 2010.

Aside from some controlled burning and microbial digestion, only upon the capping of the well did the remediation of the oil's damage truly begin. BP set up a $20 billion claims fund, which is still being administered as of March 2012. It is estimated that BP will pay $585 million in pollution violations. The company "has claimed about $40 billion in charges to cover the costs of litigation and cleanup". New CEO Bob Dudley has a difficult task ahead in continuing remediations. BP has already set aside $3.5 billion to cover expected Clean Water Act fines on the estimated 3.2 million barrels spilled. However, the ripple effect of the spill has had no small impact on the Gulf Area tourism and fishing, which has somehow gone unaccounted for in BP's legal restoration.

The legal aftermath of the spill is very consequential, as the U.S. Department of Justice (DOJ) filed a civil suit against BP and its business partners. This civil suit is expected to be followed by criminal charges–so much so that BP has already divested some assets.

Legislatively, oil companies are likely to face much more strict safety, environmental, risk management and reporting standards in the future. From the federal government level, President Obama is pushing for the cut of oil subsidies, which could lead to higher oil prices for consumers.

This type of large environmental crisis required swift corrective action and strategic public relations. There are many lessons to be learned from the way BP continues to handle the consequences of the accident and the way it employed crisis management.

Fatal Ethical Flaws

The root fatal flaws in this drilling project were not scientific in nature, but rather the tears in the fundamental ethical fabric of the team and its strategic business partners–negligence, poor risk management, and possible willful obfuscation of information for the apparent purpose of salvaging reputation, while risking the safety and well-being of BP's stakeholders.

The first ethical flaw is negligence. While some degree of mistakes is unavoidable due to human error, BP and its constituent contractors displayed a systematic failure to prevent error, which could be classified as negligence. At the time of this case, several claims had been filed against BP to this extent, but

courts have not rendered a decision and BP executives expect the case to last until at least 2014. What made the events surrounding the explosion tragic is that there were many opportunities for BP to make choices that could have prevented the disaster, but team members systematically compromised the safety and stakeholder consideration, when it cut corners to save time and to maximize profits, flying in the face of justice and utilitarianism, as discussed in the following section. This distinction is both ethically significant and economically consequential for businesses as it is embedded in our criminal law system, which penalizes on the basis of negligence.

A subset of this negligence was the failure to report safety risks, which was endemic to the broader BP contracting team, including Halliburton, Transocean, and BP staff. To this point, BP was ironically celebrating *Deepwater Horizon's* seven years of safety at the exact moment of the explosion. As this problem was so pervasive, and as the moral burden of a team's culture lies with its leadership, this implicated BP in this failure.

A third classification of ethical failure recognized by the U.S. legal system is willful misconduct, which implies a conscious and willful choice to endanger others when other options are available. Whether or not this will be found sufficiently compelling in court, this could be seen in several of BP's decisions, including its decision to drill after fracturing the well and its decision to dismiss Schlumberger before testing the well. At this point in BP's work, BP made both an ethical and financial miscalculation by actively choosing to compromise many of its stakeholders' safety, economic livelihood, environment, and personal property to maximize its own profits. This decision was systematic and was not made in isolation, suggesting abuse and grounds for liability on the part of BP and its team members.

Whether or not BP will be indicted for criminal charges, BP and nine of its business associates have faced civil charges from the DOJ in pursuit of remediation of the damages under the Oil Pollution Act and Clean Water Act. In this is an important lesson: companies like BP should consider not just the letter of the law, but the spirit of the law, such as the anti-pollution provisions of the Oil Pollution and Clean Water Acts when guiding ethical decisions. A big part of BP's damaging ethical tapestry is its failure to consider its stakeholders in driving its corporate strategy. By balancing their focus on short-term profits and considering others in their business, as well as governments, consumers, and the environment, BP's costly mistakes could also have been averted. This Stakeholder Management Approach identifies corporate strategy by mapping and evaluating the implications of strategy through the lens of stakeholder impact as shown in the following analysis. This approach is built upon "win-win" collaborative outcomes rather than short-term profits by identifying the issue at hand, by assessing the nature of stakeholder interest, by assessing each stakeholder's power, identifying stakeholder moral responsibilities, and developing the appropriate strategies and tactics. Incidentally, these same outcomes will likely save companies like BP up to billions of dollars in the long run.

Questions for Discussion

1. Who and what factors were responsible for the *Deepwater Horizon* Oil Spill?
2. Evaluate BP's corporate culture from an ethical standpoint. What role did top management have in shaping that culture?
3. What actions could/should BP management have taken in response to the many early warning signs? Did the "in action" of BP demonstrate the company's ethics? Explain.
4. What responsibility did BP's partners and oversight agencies like OSHA have in the crisis?
5. How did BP's corporate strategy affect its ethical decision making?
6. Do companies like BP should have an ethical responsibility to protect the environment? Why or why not?

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Case 7

Mattel Toy Recalls

On August 2, 2007, NBC's John Yang reported on the *Today* show a "global recall" from Fisher Price involving approximately a million toys. Presenting the initial reactions from stunned mothers, the report showed public anxiety over the risk to children's safety. That recall would be only the first of three major recalls in that month for Mattel, the parent company of Fisher Price. There had been critical steps preceding these recalls and additional actions followed.

This case describes the actions taken by key stakeholders during Mattel's three major recalls in August 2007, one of which was the largest recall ever initiated by the world's largest toy company.

Where It Began

According to Mattel executives, lead paint was discovered on some of its toys by a European retailer. On July 6, 2007, Mattel halted the production of toys at the manufacturing plant that produced the toys, while the company initiated an investigation. On July 18, Mattel gave a *New York Times* reporter a tour of the manufacturing facility in Guanyao, China, and its safety lab in Shenzhen, China. Mattel's position during the investigation was that it was unaware of whether the issue was an isolated problem or if there was a larger-scale impact.

On July 26, Mattel executives received data that confirmed there was a safety risk in 83 of their products. This prompted them to contact retailers who were distributing the affected toys. The communication was made known to the public on August 1, 2007. According to Mattel, the issue was self-identified and the Consumer Product Safety Commission was made aware of the problem. David Allmark, general manager of Fisher Price, a division of Mattel, committed to vigorously investigate and learn from the problem through the following statement: "We are still concluding the investigation, how it happened. But there will be a dramatic investigation on how this happened. We will learn from this." Allmark also indicated that the recall was accelerated, which gave Fisher Price the opportunity to quarantine approximately two-thirds of the 967,000 toys before they were sold to the public.

On August 8, Mattel identified the vendor responsible for the recalled toys. Mattel's CEO, Robert Eckert, issued the following statement during an interview regarding the contract manufacturer that produced the toys: "This is a vendor plant with whom we've worked for 15 years; this isn't somebody that just started making toys for us." In an interview, Eckert stated: "They understand our regulations, they understand our program, and something went wrong. That hurts." Mattel further communicated that they were unaware of whether the manufacturer had received materials from a certified supplier or if they had substituted materials from a non-certified supplier.

On August 11, 2007, the head of the manufacturing company linked to the Mattel recall of toys containing lead-based paint committed suicide. Zhang Shuhong, who led Lee Der Industrial Co., was found dead in his factory in China.

More Bad News

On August 14, 2007, Mattel issued two additional recalls related to toys developed by Chinese contract manufacturers. The first action was in response to a second instance of lead paint being discovered in a die cast vehicle model marketed as a character from the movie *Cars.* This recall affected 436,000 toys, all of which were manufactured by a different company than Lee Der Industrial Co. According to Mattel, the products were manufactured between May and July of 2007 and were discovered as part of a systemic review of its toy manufacturing following the initial finding of lead paint.

The second action was taken to expand the scope of an earlier recall to address 18.2 million magnetic toys that had a "design flaw." The recall included 63 types of toys that had been manufactured since 2002 and were confirmed by the Consumer Product Safety Commission as having been manufactured in China. This "design flaw" allowed small magnets to come apart from the toy with the risk of being swallowed by children. The first incident likely involved 7-year-old Paige Kostrzewski in July 2005. Kostrzewski had accidentally swallowed two magnets, which then gravitated to each other based on their magnetic pull while inside her intestines. Surgery revealed that the magnets had punctured holes in her intestines, and, according to her mother, "caused everything to just seep into her body." Luckily, Kostrzewski recovered after a two-week hospital stay and follow-up treatment to address an infection. As a result, in November 2005 Mattel voluntarily recalled 4.4 million of the models, 2.5 million of which were in the United States.

With regard to the August 14 recalls, Nancy A. Nord of the Consumer Product Safety Commission indicated that no recent injuries had been reported for the products being recalled and that the action was "intentionally broad to prevent injuries." However, previous recalls in November 2005 of the magnetic "design flaw" in Polly Pocket toys did include injuries. Specifically, 19 children have required surgery and one child has died since 2003. According to the *New York Times* article titled "Mattel Recalls 19 Million Toys Sent from China," published on August 15, 2007, Mattel executives had stated the previous day that "in the long run [we] are trying to shift more of [our] toy production into factories [we] own and operate–and away from Chinese contractors and sub-contractors." However, the same article clarified that the cause of the recall was based on a design flaw, and that while the Chinese manufacturers were producing the toys, the design of the product was developed by Mattel–who is ultimately responsible for the specification.

What Took So Long?

Following the recalls, public speculation grew as to whether Mattel could have warned the public of these safety risks any earlier. Gerrick Johnson, an analyst with BMO Capital Markets, felt that Mattel could have: "You have to alert the public right away. I think it's a public relations nightmare more than anything else." Other analysts believe the company has been proactive and transparent. Sean McGowan, an analyst at Wedbush Morgan Securities Inc. felt Mattel

would achieve a "long-term trust" as a result of it "being honest about investigating any other problems."

According to the *Wall Street Journal* article titled "Safety Agency, Mattel Clash over Disclosures," the Consumer Product Safety Commission has a policy that requires manufacturers to report "all claims of potentially hazardous product defects within 24 hours, with few exceptions." In the case of the recall of 18 million magnetic toys, Mattel took months to collect and analyze data and reports before notifying the agency. Companies that produce similar toys as Mattel, with magnetic components, have worked with the Consumer Product Safety Commission since early 2006.

Based on the company's history, this noncompliance represents a systemic practice. The company has been fined twice for what was described as "knowingly withholding information regarding problems that "created an unreasonable risk of serious injury or death."

The first incident was related to a failure to report a fire hazard in a timely manner for its Power Wheels motorized toys, which were intended to be ridden by children aged two years or older. According to Ann Brown, chair of the Consumer Products Safety Commission, Mattel knew of the risk to children's safety, however "did nothing for years." The penalty for not reporting the hazard to the agency was assessed in 2001 after a recall of 10 million toys in 1998. According to the agency, there were approximately 150 reports of fires in the Power Wheels cars, as well as up to 10 times that number of complaints for overheating and other deficiencies prior to the company issuing the recall. The Consumer Product Safety Commission remained skeptical of Mattel's handling of the Power Wheels recall, and initiated at least nine different investigations into whether problems had occurred following the recall.

The second fine was issued for a problem that occurred just a year after the Power Wheels penalty. In 2002, Mattel became aware of issues with its Little People Animal Sounds Farm. The complaints claimed that tiny screws used in the farm could become loose and pose the risk of a child accidentally swallowing them. In an investigation conducted by the U.S. government, it was determined that Mattel was made aware of 33 reports of this safety hazard—including one instance of a baby swallowing the screw, which required emergency surgery—before informing the Consumer Product Safety Commission. Mattel reached a settlement of $975,000 yet denied any wrongdoing. A recall of the product was initiated in April 2003.

Mattel is also under scrutiny for the more recent recalls involving the 18 million units of toys containing magnetic components. Between the initial Polly Pocket recall in November 2006 and the expanded recall of August 2007 for the same issue, Mattel received an additional 400 reports of similar magnetic hazards with different toys. It is not currently known how long Mattel waited before notifying the agency of these reports. The Consumer Product Safety Commission is currently investigating Mattel on the timeliness of its reporting practices and has not made that information public. However, when Mattel CEO Robert Eckert was asked in September 2007 of the date of disclosure for the magnetic

component recall, he responded that "he couldn't remember when the company brought the complaints about the magnets to the attention of authorities."

While there have been specific cases of untimely disclosures from Mattel, there have also been comments issued from Eckert rationalizing Mattel's untimely practice and justifying its position for waiting extended periods before notifying the agency and the public. Eckert has claimed that the company discloses problems on its own timetable, due to a belief that the regulatory requirements are "unreasonable." Furthermore, Eckert claimed that Mattel should have the ability to evaluate any reports of safety hazards prior to reporting them to the agency or the public. The Consumer Product Safety Commission disagreed in a statement issued by the agency's spokesperson, Julie Vallese: "It's a statute; it's clear." In late 2007, the agency initiated a formal investigation into the timeliness of Mattel's hazardous incidents reporting process to examine its more recent disclosures.

The Aftermath

Following the lead paint recall on August 1, 2007, Mattel communicated that it would evaluate methods of addressing the problem. CEO Eckert indicated that this would include the possibility of reducing the amount of toys it produces through contract manufacturers. In what appeared to be an attempt at distancing the company from its Chinese contract manufacturers, Eckert issued the following statement: "I, like you, am deeply disturbed and disappointed by recent events. We were let down, and so we let you down."

Despite comments that deflected a portion of the responsibility, Eckert also made statements following the second cycle of recalls issued on August 14 that attempted to appease consumers and regain their trust. In a full-page advertisement taken out in major newspapers such as the *New York Times, USA Today,* and the *Wall Street Journal,* Eckert stated: "Our long record of safety at Mattel is why we're one of the most trusted names with parents, and I am confident that the actions we are taking now will maintain that trust."

Following the initial comments issued by Mattel, Chinese manufacturers defended themselves against inferences that U.S. companies did not share the blame. The following statement was issued by China's General Administration of Quality Supervision, Inspection, and Quarantine: "Chinese original equipment manufacturers were doing the job just as importers requested, and the toys conformed with the U.S. regulations and standards at the time of the production." Specific to Mattel, the organization stated: "Mattel should improve its product design and supervision over product quality."

In September 2007, Mattel seemed to agree with the Chinese position, and launched a public relations campaign to issue a formal apology to those in China whose reputations were affected. Mattel's executive vice president for worldwide operations, Thomas Debrowski, met with the head of Chinese Product Safety, Li Changjiang, to issue the following statement: "Mattel takes full responsibility for these recalls and apologizes personally to you, the Chinese people, and all of our customers who received the toys." Debrowski went on to specifically identify

the design flaw as the root cause of the magnetic-component-based recall: "The vast majority of those products that were recalled were the result of a design flaw in Mattel's design, not through a manufacturing flaw in China's manufacturers."

In addition, the company issued a formal statement which referenced the lead paint recall as well. The statement called the scope of the recall "overly inclusive, including toys that may not have had lead in paint in excess of the U.S. standards." The statement continued, "The follow-up inspections also confirmed that part of the recalled toys complied with the U.S. standards."

On September 12, 2007, a congressional hearing was held to attempt to identify what needed to be done to ensure that the types of recalls issued by Mattel do not continue. Congress assigned equal blame to all parties across the board, including Chinese safety standards, Mattel, and the Consumer Product Safety Commission.

Mattel recognized its level of responsibility through a response from Eckert: "We are by no means perfect." Mattel continued that it would rectify the situation by taking steps such as better oversight of quality controls for its contract manufacturers and instituting its own laboratories for testing of its products.

The Consumer Product Safety Commission has conceded that it is understaffed. From 1974 to 2007, the agency's employee number has been reduced from 800 to 400. What is even more alarming is that there is only one resource dedicated to the actual testing of toys.

The Chinese manufacturers were also identified by Congress. Republican senator Sam Brownback of Kansas concluded that "'Made in China' has now become a warning label." Brownback continued: "We're seeing this in the charts and we're seeing it in the products and it's got to stop."

While the fallout from the 2007 toy recalls will continue for Mattel and all parties involved, the result will likely be stricter policy, stronger internal quality controls, and improved subcontractor oversight, all of which will ultimately benefit consumer safety. Mattel Toys has not had a recall since this debacle.

Stricter Legislation

In a response to the Mattel Toys recalls, the Consumer Product Safety Improvement Act of 2008 was passed. According to http://CPSC.gov:

> The Consumer Product Safety Improvement Act (CPSIA) of 2008 requires that nearly all children's products:
>
> a) comply with all applicable children's product safety rules;
> b) are tested for compliance by a CPSC-accepted laboratory;
> c) have a written Children's Product Certificate (issued by the manufacturer or importer) that provides evidence of the product's compliance; and
> d) have permanent tracking information affixed to the product and its packaging.
>
> The CPSIA also requires domestic manufacturers or importers of non-children's products (cpsc.gov/generaluse) for which a consumer product safety rule, or any similar rule, ban, standard, or regulation under any law enforced by the CPSC

is in effect, to issue a "General Certificate of Conformity" (cpsc.gov/gcc). The GCC must be based on a test of each product or a reasonable testing program.

Ironically, however, Mattel Toys received a reprieve on item b in this law. Mattel-owned laboratories have been deemed "firewalled third-party laboratories" and therefore, Mattel Toys can use their own laboratories for testing mandated by this Act.

Questions for Discussion

1. Identify the major stakeholders in the case. Who was responsible for what went wrong and why?
2. What are the ethical issues in the case, and for whom?
3. Do you think cross-cultural dynamics and misunderstandings played a role in the resulting problems in the case? Explain.
4. Was there a prodromal (precrisis) phase in this case? If so, identify this stage and the event(s) that explain it.
5. Which issues management framework would you suggest to best explain this case? Why?
6. Is it ethical that Mattel is partially exempt from the Consumer Product Safety Improvement Act of 2008? What signal and impact would this exemption send to and have on the industry?

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Case 8

Genetic Discrimination

Genetic discrimination is defined by the Centers for Disease Control and Prevention as "prejudice against those who have or are likely to develop an inherited disorder." Advances in science make possible the determination of whether specific gene mutations exist, and the ability to discover the likelihood of an individual developing a disorder based on the existence of these mutations. These developments have created situations that concern the public: their privacy and possible employment livelihood. One of the major issues noted by the National Human Genome Research Institute (NHGRI) is the possibility that individuals who have taken this testing, and received positive results, will be turned down for health insurance or employment. This possibility will most probably be at issue depending on the political party and dominant political persuasion in power at both the national and state levels, as well as with the Supreme Court.

Many people with family histories or other factors that determine their susceptibility to certain diseases or disorders will have to make a decision about whether to be tested for the existence of certain genetic sequences or mutations. A major factor in this decision will be how this information will be used and who will be able to access the results. Patients may choose to refuse testing that could save their lives or improve their quality of life because they fear future discrimination. Employers with group insurance plans may want to know whether any of their employees are predisposed to a specific disorder. Insurance providers would also like to have the results of genetic testing to assist in underwriting policies. Both of these scenarios are likely to lead to discrimination against or exclusion of certain individuals for either employment or insurance coverage.

Human Genome Project

One of the major catalysts of the advancement of genetic testing and the interpretability of genetic information was the Human Genome Project. The Human Genome Project began in 1990 as a joint effort between the National Institutes of Health and the United States Department of Energy. The project had six goals: (1) to identify all of the approximately 20,000–25,000 genes in human DNA; (2) to determine the sequence of the 3 billion chemical base pairs that make up human DNA; (3) to store this information in databases; (4) to improve tools for data analysis; (5) to transfer related technologies to the private sector; and (6) to address the ethical, legal, and social issues (ELSI) that may arise from the project. In addition to helping meet these goals, accomplishments leading to the project's completion in 2003 have also contributed to major advances in scientific research and health care, primarily in the areas of medicine and genetic testing. Understanding the genes and sequences associated with common diseases has future implications for the entire human population, and will help to detect and possibly remedy disorders with more precise and targeted treatments.

Business Response

Even before the entire human genome had been sequenced and published, and the implications of the discovery had been reviewed to establish guidelines and boundaries, biotechnology companies and others conducting scientific research had begun to develop uses for this new way of looking at human conditions and diseases. One question from this new branch of medical technology is who, if anyone, should own gene sequences and who has the rights to one's genetic information? The issue of patenting gene sequences began long before the map of the human genome was completed and prior to consequences of granting these patents were able to be seriously examined. Companies had already begun to submit applications and receive approval for gene sequences that had some still unknown future use and potential profitability. According to Modern Drug Discovery contributor, Charles W. Schmidt, "[T]hose who seek patents usually want to protect research investments in one of two markets: gene- and protein-based drug development or diagnostic testing that searches for gene sequences linked to a given illness." Even without strong federal regulations to guide the use and ownership of test data and eliminate the reluctance of people to agree to testing, companies developing genetic tests believed that patenting is necessary to protect an industry that is someday likely to generate millions in profits. Those in opposition to this view have trouble allowing ownership of something that is so personal. The major caveat to granting these patents is that it limits and slows the competition in the industry to find uses for and make advances in an already patented gene sequence. However, if there is no guarantee of exclusive ownership with the outcome of research, companies may choose not to move forward in research. The main issue of a significant business response to scientific advancements in genetic testing and gene sequencing is ensuring that laws and regulations keep up with technology and medical advances to prevent major abuse, ownership, and privacy issues.

Two following cases illustrate the evolution between 2001 and 2013 of EEOC (Equal Employment Opportunity Council) enforcement with regard to the genetic nondiscrimination Title II law.

The Burlington Northern and Santa Fe Railroad Case

In February 2001, the Equal Employment Opportunity Commission (EEOC) filed a suit against the Burlington Northern and Santa Fe Railroad for secretly testing some of its employees. The genetic tests conducted had been developed by Athena Diagnostics in Worcester, Massachusetts, to detect a rare neuromuscular disorder, but Burlington Northern had been using them to validate and predict claims of carpal tunnel syndrome made by railroad workers. This incident, and others like it across the United States and Europe over the following years, raised concerns about the access and rights that employers have to their employees' medical and genetic information. In this case, if Burlington Northern had discovered that employees with carpal tunnel syndrome had a genetic predisposition to the injury, the company could have claimed that the ailment was not job related and therefore denied payment of any medical bills. The EEOC filed its suit

referencing the American Disabilities Act's statement that "it is unlawful to conduct genetic testing with the intent to discriminate in the workplace." Cases like this alerted lawmakers and activists to the growing concerns of discrimination in the workplace based on genetic information, and upon closer examination of the issue, revealed significant inconsistencies and gaps in the laws currently protecting the rights of employees.

The following lawsuit is the first initiated by the EEOC to effectively enforce GINA (Genetic Information Nondiscrimination Act of 2008). This case and the previous one summarized above (Burlington Northern Santa Fe Railway Company in Fort Worth, Texas, also for carpal tunnel syndrome in April 2001) emphasize the integral relationship between conduct prohibited under GINA and conduct prohibited under the Americans with Disabilities Act of 1990 as amended (42 U.S.C. §12101 et seq., Pub. L. 101-336). "GINA Title II prohibits both the acquisition and the use of genetic information in employment contexts."

Rhonda Jones

Rhonda Jones was a temporary memo clerk for Fabricut, Inc. Her temporary employment was running out when she applied for a permanent position with Fabricut. The Company at first offered her the position before violating the GINA Title II law when, as part of its pre-employment medical examination, it allegedly requested Rhonda Jones' family history with regard to several specific conditions. "GINA defines 'genetic information' broadly to include family medical history." Based on the pre-employment medical examination, Fabricut allegedly "required Jones to obtain additional testing to rule out carpal tunnel syndrome (CTS)." Even though later testing did rule out CTS, because of information she gave the company, Fabricut allegedly withdrew their job offer "on the basis of the pre-employment medical examination and its view that she had CTS."

"As part of the consent decree settling the case, Fabricut agreed to pay $50,000 in damages. The company also agreed to undertake corrective actions that include posting a non-discrimination notice to employees. GINA requires that employers post a non-discrimination notice, and 'Equal Employment Opportunity is the Law' posters are readily available on the EEOC web site. Fabricut also agreed to have its employees responsible for hiring decisions undergo non-discrimination training and further agreed to distribute non-discrimination policies to its employees."

Government Response to Advances in Genetic Testing and Discrimination

As with most human resource issues, companies cannot always be trusted to act in the best interests of their individual employees, especially where privacy rights are concerned. Throughout the past two decades, the United States has drafted and passed several laws addressing the issue of discrimination by employers and private businesses, and protecting employees who speak out against discriminatory behavior. One of the most well-known regulations in this category is the Americans with Disabilities Act of 1990 (ADA), which prohibits

discrimination in hiring on the basis of a disability. Similarly, Title VII of the Civil Rights Act of 1974 prohibits employment discrimination on the basis of race, color, religion, sex, and national origin. According to National Institutes of Health Consultant Robert B. Lanman, J.D., who was commissioned in May 2005 by the Secretary's Advisory Committee on Genetics, Health, and Society to examine the adequacy of current laws protecting against genetic discrimination, these laws have not been updated to specifically relate to genetic discrimination. They offer protection to the extent that a genetic predisposition is common in a specific race or other group protected under the ADA or Civil Rights Act. In his executive summary, Lanman offered the example of Tay-Sachs disease, which is prevalent in persons of Eastern European Jewish ethnicity. Discrimination based on the genetic information of an individual that is unrelated to an individual's race or ethnicity would not currently fall under the protection of the ADA or Civil Rights Act.

A major section of the pieced-together legislation that is currently protecting citizens from genetic discrimination is the Health Insurance Portability and Accountability Act of 1996 (HIPAA). This act prohibits insurance companies from (1) excluding members because of a preexisting condition that is based solely on the results of genetic testing or family history, (2) imposing eligibility requirements, or (3) restricting coverage based on genetic information. HIPAA does not restrict insurance companies from "requesting, purchasing, or otherwise obtaining genetic information about an individual," and it does not restrict insurance companies from charging higher premiums or including this genetic information in the underwriting process.

The major problem with the state and federal regulations enacted to date is that genetic information is either not mentioned as a basis for discrimination, or it is not defined consistently throughout existing laws. The United States has two primary concerns: protecting the privacy of genetic information, and preventing discrimination based on genetic information—especially by employers and insurance companies. To address this issue, new federal regulation must cover gaps left in existing directives and account for future developments in the industry. The hodgepodge of existing laws combined with the inconsistency of state laws leaves too many loopholes to provide comprehensive protection for the general public.

The Genetic Information Nondiscrimination Act of 2005

On February 17, 2005, the Senate passed S.306, the "Genetic Information Nondiscrimination Act of 2005" with a vote of 98–0. The law was then passed on to the House of Representatives on March 10, 2005, where it was referred to the Subcommittee on Health. No further action has been taken, and the bill has not yet become a law. The proposed bill specifically "prohibits discrimination on the basis of genetic information with respect to health insurance and employment." In addition, it amends the Employee Retirement Income Security Act of 1974 (ERISA) and the Public Health Service Act (PHSA) to include in their definitions of genetic information, any results of genetic testing and information

pertaining to whether or not testing was performed. It would also disallow insurance companies from adjusting premiums based on the results of genetic testing, and prevents them from requiring genetic tests for subscribers or their dependents. The law concludes by covering fines and penalties and calls for a commission to review advances in science and technology and developments in genetic testing six years after the enactment of the law to make recommendations and amendments. This bill in 2005 was considered dead in the House of Representatives but was resubmitted for consideration in 2007.

One possible reason for not yet signing the Genetic Information Nondiscrimination Act is resistance from the Health Insurance Association of America (HIAA), and the claim that additional federal regulation is not needed. Opponents of the bill see sufficient restrictions in the current existing laws, and do not see the necessity of new legislation. However, Lanman's report, "An Analysis of the Adequacy of Current Law in Protecting Against Genetic Discrimination in Health Insurance and Employment," points out several shortcomings in the combined efforts to protect individuals from this type of discrimination. More importantly, future advances in bio- and medical technology need to be accounted for–and somewhat are–by this new proposed bill.

The bill's consequences for employers and health insurance providers are focused around the idea of being informed. Since health insurance costs are rising, and they are likely to continue to rise due to advances in medicine, testing, and the ability to prolong life, employers must be more aware of the costs of hiring additional employees. Health insurance providers also must remain competitive in balancing the cost of providing health care coverage and mitigating the financial risk to themselves. If employers and health insurance providers are not privy to all of the information available concerning the insured parties, premiums will not be fair or balanced.

While the health insurance companies will probably not come out ahead in this battle, some of their concerns should be taken into consideration if the bill is to be amended before it is passed. For example, one of the members of the Human Genome Project's Committee for Ethical, Legal, and Social Implications, Nancy L. Fisher, MD, asks if genetic testing and health insurance can coexist. Fisher's main concern is the definition of terms like "preexisting condition" and "genetic information," and how new laws will affect not only the health insurance industry, and its ability to survive, but also the financial cost for taxpayers if "society decides that everyone is entitled to comprehensive health care."

May 21, 2008: The Genetic Information Nondiscrimination Act

The Genetic Information Nondiscrimination Act (GINA), referred to as "the first civil rights legislation of the 21st century" was reintroduced to Congress and became a law on May 21, 2008. The law prevents employers and insurers from using genetic data against individuals and employees. The law states that (1) employers cannot deny a person a job because s/he is genetically predisposed to develop a particular disease or condition; (2) insurers cannot use an individual's genetic profile to deny coverage or raise his/her premiums; and (3) now

protected, an individual benefits from medical genetic testing without concern with regard to results being used against him/her. However, the law does not protect third parties from using an individual's genetic results, including the military. It is also plausible that an individual may still be at risk of being discriminated against with regard to health insurance.

Title II GINA Law now

As stated earlier, the two cases presented, 2001 and 2013, illustrate the difference in EEOC's effectiveness in enforcing the Title II GINA law. Given the history of disputes over genetic testing, ownership and commercialization of genetic tests and research results, and employees at risk and who may or may not have a preexisting genetic condition, at present, this federal law appears to be serving its intended purpose.

Questions for Discussion

1. What is genetic discrimination, and why is it an issue?
2. Who would benefit and who would be at risk if genetic testing and the results of such tests were legal and could be required of employees? Explain.
3. Explain the ethical principle(s) that could be used to (a) argue against genetic testing of employees and (b) argue for genetic testing.
4. Explain your position on the issue of genetic testing by employers.
5. How does the outcome of Rhonda Jones' case affect employers? Is there now a fair balance between the Title II GINA law and employers? Explain.

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4

THE CORPORATION AND EXTERNAL STAKEHOLDERS

Corporate Governance: From the Boardroom to the Marketplace

4.1 Managing Corporate Social Responsibility in the Marketplace

Ethical Insight 4.1

Point/CounterPoint

4.2 Managing Corporate Responsibility with External Stakeholders

Ethical Insight 4.2

4.3 Managing and Balancing Corporate Governance, Compliance, and Regulation

Ethical Insight 4.3

4.4 The Role of Law and Regulatory Agencies and Corporate Compliance

4.5 Managing External Issues and Crises: Lessons from the Past (Back to the Future?)

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Questions

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9. Conscious Capitalism: What Is It? Why Do We Need It? Does It Work?
10. Goldman Sachs: Hedging a Bet and Defrauding Investors
11. Google Books

Notes

OPENING CASE

When you read "The TJX Companies, Inc. V.A.L.U.E. Corporate Social Responsibility Report 2013" and see Carol Meyrowitz's letter, you would never believe the crisis that rocked the company in 2008 ever happened. This case illustrates one difference between companies that learn, change, and grow, and those that do not.

TJX seems to practice its VALUE proposition, "Vendor Social Compliance, Attention to Governance, Leveraging Differences, United With Our Communities and Environmental Initiatives." Forbes reported in 2013 that the TJX Companies (NYSE: TJX) has taken over the #95

spot from Capital One Financial Corp (NYSE: COF). Although the company, as with several other retailers, could improve its customer satisfaction index score, it has recovered from the 2008 crisis recounted here.[1]

On January 17, 2008, TJX Companies, Inc., a leading retailer in the field of clothing and home fashions that operates stores domestically and internationally, announced that the organization had experienced an unauthorized intrusion of its computer systems.[2] Customer information, including credit card, debit card, and driver's license numbers, had been compromised. This intrusion had been discovered in December of 2006, and it was thought that data and information as far back as 2003 had been accessed and/or stolen. At the time, approximately 45.6 million credit card numbers had been stolen. In October of 2007, the number rose to 94 million accounts.[3] This is one of the largest credit card thefts or unauthorized intrusions in recent history.

Because of the lax security systems at TJX, the hackers had an open doorway to the company's entire computer system. In 2005, hackers used a laptop outside of one of TJX's stores in Minnesota and easily cracked the code to enter into the Wi-Fi network. Once in, the hackers were able to access customer databases at the corporate headquarters in Framingham, Massachusetts. The hackers gained access to millions of credit card and debit card numbers, information on refund transactions, and customer addresses and phone numbers. The hackers reportedly used the stolen information to purchase over $8 million in merchandise.[4]

TJX used an outdated WEP (wired equivalent privacy) to secure its networks. In 2001, hackers were able to break the code of WEP, which made TJX highly vulnerable to an intrusion. (Similar data breaches have occurred within the past few years at the firms ChoicePoint and CardSystems Solutions.) In August of 2007, a Ukrainian man, Maksym Yastremskiy, was arrested in Turkey as a potential suspect in the TJX case. According to police officials, Yastremskiy is "one of the world's important and well-known computer pirates."[5] He led two other men in the scheme.[6]

Even though the intrusion was discovered in December of 2006, the company did not publicize it until a month later. Consumers felt that they should have been notified of the breach once it was discovered. However, TJX complied with law enforcement and kept the information confidential until it was told it could notify the public. Retail companies such as TJX that use credit card processing are required to comply with the Payment Card Industry Data Security Standard (PCI DSS). The PCI DSS is a set of requirements with the purpose of maximizing the security of credit and debit card transactions. A majority of firms have not complied with this standard, as was the case with TJX.

A number of stakeholders were involved in this break-in: consumers, who were put at great risk; banks; TJX (its shareholders, management, employees, and other internal parties who did business with and were invested in the firm); the credit card companies; the law enforcement and justice systems; the public; other retail firms; and the media, to name a few. Chief executive officer (CEO) Carol Meyrowitz took an active role in informing the public in statements on the company's web sites and through the media about the company's responsibility and obligations to its stakeholders during and after the investigation. TJX also contacted various agencies to help with the investigation. A web site and hotline were established to answer customer questions and concerns.

The intrusion cost TJX approximately $118 million in after-tax cash charges and $21 million in future charges. Although TJX incurred substantial legal, reimbursement, and improvement costs, the company's pretax sales were not negatively affected. Sales during the second quarter of fiscal year 2008 increased compared to second quarter sales from fiscal year 2007.[7]

At the end of 2007, TJX reached a settlement agreement with six banks and bankers' associations in response to a class action lawsuit against the company.[8] In the spring of 2008, TJX settled in separate agreements with Visa ($40.9 million with 80% acceptance) and MasterCard International (a maximum of $24 million with 90% minimum acceptance). There was almost full acceptance of the alternative recovery offers by eligible MasterCard accounts.[9] Note that those issuers who accept the agreements and terms "release and indemnify TJX and its acquiring banks on their claims, the claims of their affiliated issuers, and those of their sponsored issuers as MasterCard issuers related to the intrusion. That includes claims in putative class actions in federal and Massachusetts state courts."[10]

Affected customers were reimbursed for costs such as replacing their driver's licenses and other forms of identification and were offered vouchers at TJX stores and free monitoring of their credit cards for three years. Customer discontent was reportedly expressed after the intrusion; however, customer loyalty returned,[11] as was evidenced in sales numbers.

4.1 Managing Corporate Social Responsibility in the Marketplace

Corporate social responsibility (CSR) involves an organization's duty and obligation to respond to its stakeholders' and the stockholders' economic, legal, ethical, and philanthropic concerns and issues.[12] This definition encompasses both the social concerns of stakeholders and the economic and corporate

interests of corporations and their stockholders. Generally, society cannot function without the economic, social, and philanthropic benefits that corporations provide. Leaders in corporations who use a stakeholder approach commit to serving broader goals, in addition to economic and financial interests, of those whom they serve, including the public.

Managing CSR in the marketplace with multiple stakeholder interests is not easy. As discussed in Chapter 2, ethics at the personal and professional levels requires reasoned and principled thinking, as well as creativity and courage. When ethics and social responsibility escalate to the corporate level, where companies must make decisions that affect governments, competitors, communities, stockholders, suppliers, distributors, the public, and customers (who are also consumers), moral issues increase in complexity, as this chapter's opening case illustrates. For organizational leaders and professionals, the moral locus of authority involves not only individual conscience but also corporate governance and laws, collective values, and consequences that affect millions of people locally, regionally, and globally. Patagonia, for example, is a company that conducts its outdoor apparel business with a 360-degree focus of responsibility. The company takes responsibility for the actions of all members of its supply chain and for impacts on the environment. This attitude is integrated into the culture of the company, its organizational structure (with a new Director of Social/Environmental Responsibility position created in 2010), and its relationship with suppliers. It has developed a "contractor relationship assessment," a scorecard system that is used to rate the performance of each factory. Patagonia, along with many other companies, now recognizes a broader scope of accountability and the interests of multiple stakeholders.[13]

In the opening case, the TJX executives had to deal not only with their own customers, but with banks (in a class action suit), credit card companies, the media, competitors, and a network of suppliers and distributors—as well as their own reputation. What may have seemed like a routine technical security problem turned into the largest-known credit card theft/unauthorized intrusion in history. Had the CEO not stepped in and become a responsible spokesperson and decision maker for the company, customers may not have responded in kind.

The basis of CSR in the marketplace begins with a question: What is the philosophical and ethical context in which CSR and ethical decisions are made? For example, not everyone is convinced that businesses should be as concerned about ethics and social responsibility as they are about profits. Many believe that ethics and social responsibility are important, but not as important as a corporation's performance. This classical debate—and seeming dichotomy—between performance, profitability, and "doing the right thing" continues to surface not only with regard to CSR, but also in political parties and debates over personal and professional ethics. The roots of CSR extend to the topic of what a "free market" is and how corporations should operate in free markets. Stated another way, does the market sufficiently discipline and weed out inefficient "bad apples" and wrongdoers, thereby saving corporations the costs of having to support "soft" ethics programs?

Ethical Insight 4.1

Ethical Issues in the TJX Case

After reading the opening case, answer and be prepared to discuss in class these questions:

1. If you had been assigned to investigate, report, and offer recommendations from this case, how would you respond to this question: Who was to blame for the security breach and why?
2. Which factor, in your judgment, was the most important contributor to TJX's security breach: the lack of a comprehensive security policy and legal procedures OR issues with the company's corporate leadership and culture? Explain.
3. What will work best for TJX in this case: discipline from the legal and judicial system OR required changes in the company's leadership and culture regarding security? Explain.

The type of information security breach experienced by TJX has become almost commonplace for large organizations, particularly with business trends toward electronic data collection and storage and the increasing complexity of technology. Corporations now have an ethical responsibility for preventive, detective, and corrective actions regarding the protection of stakeholder information. The following is a list of the top ten "massive security breaches" of recent years:[14]

1. *TJX (February 2007).* "Thieves had stolen information on possibly tens of millions of credit and debit cards. The company first thought its systems had been compromised for about eight months, but it turned out the vulnerability might have lasted for almost a year longer than that. The incident wound up costing TJX millions of dollars paid to the Federal Trade Commission (FTC), credit card companies, banks, and customers. Eleven hackers were eventually arrested for the break-in. Security breaches have only increased in scope and frequency in recent years, as more businesses store their data in digital files and thieves become increasingly sophisticated in how they gain access to those files."

2. *CardSystems Solutions (June 2005).* "MasterCard announced that up to 40 million credit card holders were at risk of having their data stolen—and 200,000 definitely had. CardSystems Solutions had improperly stored the card data, unencrypted, in order to do research on the transactions."

3. *Heartland Payment Systems (2009).* "The company revealed that tens of millions of transactions might have been compromised. The company's computers were infected with malware."

4. *Bank of New York Mellon (February 2008).* This was an instance of "a physical security breach rather than an electronic one, the Bank of New York Mellon simply lost a tape. The company sent 10 unencrypted backup tapes to

a storage facility. When the storage firm's truck arrived at the facility, however, only nine tapes were still on board. The missing tape contained social security numbers and bank account information on 4.5 million customers."

5. *Hannaford Brothers (March 2008).* "Hackers had gained access to more than 4.2 million credit card transactions. By the time word got out, more than 1,800 of the credit card numbers had already been used at company stores. The breach resulted in two class action lawsuits on behalf of customers."

6. *HM Revenue and Customs (November 2007).* "Two computer discs holding personal information on 25 million British citizens had been lost in the mail. The discs had been sent by courier via the HMRC's internal mail system."

7. *U.S. Department of Veterans Affairs (2009).* The agency sent a troubled hard drive out for repair without first erasing the unencrypted data contained on the disc—personal information for about 76 million veterans.

8. *Certegy (2007).* An employee of this subsidiary of Fidelity National Information Service "had been stealing customer records and selling them to a data broker. The records included credit card, bank account, and other personal information, and Certegy estimated the breach affected 8.5 million customers. Certegy wound up out nearly $1M in donations and court costs."

9. *Oklahoma Department of Human Services (April 2009).* Someone removed a laptop containing unencrypted client records from the office. "They left the laptop in their car, someone broke into the car, and the names, social security number, and other sensitive information on about a million Oklahomans went missing."

10. *Health Net (May 2009).* "The Connecticut health care provider reported that an unencrypted portable storage device was missing, containing seven years' worth of financial and medical information on 1.5 million customers. The Connecticut attorney general promptly filed suit. Health Net settled for $250,000."

Free-Market Theory and Corporate Social Responsibility

Free-market theory holds that the primary aim of business is to make a profit. As far as business obligations toward consumers, this view assumes an equal balance of power, knowledge, and sophistication of choice in the buying and selling of products and services. If businesses deliver what customers want, customers buy. Customers have the freedom and wisdom to select what they want and to reject what they do not want. Faulty or undesirable products should not sell. If businesses do not sell their products or services, it is their own fault. The marketplace is an arena of arbitration. Consumers and corporations are protected and regulated—according to this view—by Adam Smith's (one of the modern founders of capitalism) notion of the "invisible hand." What would have happened to TJX customers without regulation?

Several scholars argue that Adam Smith's "invisible hand" view is not completely oriented toward stockholders. For example, Eugene Szwajkowski argues that "Smith's viewpoint is most accurately positioned squarely between those who contend firms should act out of self-interest and those who believe

corporations should be do-gooders. This middle ground is actually the stakeholder perspective. That is, stakeholders are in essence the market in all its forms. They determine what is a fair price, what is a successful product, what is an unacceptable strategy, what is intolerable discrimination. The mechanisms for these determinations include purchase transactions, supplier contracts, government regulation, and public pressure."[15] Szwajkowski continues, "Our own empirical research has clearly shown that employee relations and product quality and safety are the most significant and reliable predictors of corporate reputation."[16]

Economist and free-market advocate Milton Friedman is noted for a philosophical view summarized in the following quote: "The basic mission of business [is] thus to produce goods and services at a profit, and in doing this, business [is] making its maximum contribution to society and, in fact, being socially responsible."[17] Friedman more recently stated that even with the recent corporate scandals, the market is a more effective way of controlling and deterring individual wrongdoers than are new laws and regulations.[18]

Free markets require certain conditions for business activity to help society. These conditions include (1) minimal moral restraints to enable businesses to operate and prevent illegal activities such as theft, fraud, and blackmail; (2) full competitiveness with entry and exit; (3) relevant information needed to transact business available to everyone; and (4) accurate reflection of all production costs in the prices that consumers and firms pay (including the costs of job-related accidents, injuries from unsafe products, and externalities, which are spillover costs that are not paid by manufacturers or companies, but that consumers and taxpayers often pay, e.g., pollution costs). Legal and ethical problems arise when some or all of these conditions are violated, as in this chapter's opening case.

Problems with the Free-Market Theory

Although the free-market theory continues to have its advocates, controversy also exists regarding its assumptions about stakeholders and consumer–business relationships. For example, consider these arguments:

1. Most businesses are not on an equal footing with stakeholders and consumers at large. Large firms spend sizable amounts on research aimed at analyzing, creating, and—some argue—manipulating the demand of certain targeted buyers and groups. Children and other vulnerable groups, for example, are not aware of the effects of advertising on their buying choices.

2. As discussed in Chapter 5, it has been questioned as to whether many firms' advertising activities truthfully inform consumers about product reliability, possible product dangers, and proper product use. A thin line exists between deceit and artistic exaggeration in advertising.

3. The "invisible hand" is often nonexistent for many stakeholders and, in particular, for consumers in need of protection against questionable, poorly manufactured products that are released to market. One reason a stakeholder

view has become a useful approach for determining moral, legal, and economic responsibility is that the issues surrounding product safety, for example, are complex and controversial.

Another important argument against free-market theory is based on what economists refer to as "imperfect markets," that is, markets in which competition "is flawed by the ability of one or more parties to influence prices."[19]

Intermediaries: Bridging the Disclosure Gap

Inequality of information available to companies and stakeholders is attributable in part to imperfect markets. Investors, for example, rarely have access to complete information to make investment decisions. They must settle for incomplete and/or inaccurate information. The presence of "intermediaries" can help managers and other designated officers obtain accurate information that might otherwise be willfully withheld and/or manipulated for personal gain or misplaced and lost from neglect.

Two general types of intermediaries are financial and information. *Financial intermediaries* include venture capitalists, banks, and insurance companies; *information intermediaries* include auditors, analysts, rating agencies, and the press. These intermediaries obtain information to provide stakeholders with a more complete and accurate financial picture of the company's position in markets. Intermediaries can prevent leaders and managers of companies from taking unfair advantage of imperfect markets by intentionally failing to disclose information to relevant stockholders and stakeholders. The Lehman Brothers, for example, used what is called a "Repo 105" scheme to falsely increase their balance sheet by billions of dollars, thereby misleading stakeholders in and since 2007. This scheme involved repurchase agreements, in which Lehman Brothers entered into agreements to "sell" and then "buy back" toxic assets from other banks. This secretive process misled investors since the company recorded the agreements as sales and removed the bad assets from the financial statements, thus showing stakeholders incorrect and misleading information about the company's financial performance. Lehman had more information than its stakeholders and intentionally chose not to disclose its complete and accurate books.[20]

Another example of imperfect and skewed market power occurs in Africa, "where a few pharmaceutical companies effectively control the availability of several key drugs. In effect, they are beyond the financial means of millions of Africans or their governments. When a few dominating companies cut the prices of several key ingredients of the AIDS cocktail, they demonstrated this power. But this also revealed a further imperfection in the real market, where only rickety systems, if any, exist to deliver the drugs to patients requiring sophisticated and continuous follow-up care."[21]

Mixed-Market Economies

The debate regarding free markets, imperfect markets, and other forms of social organization is interesting but not always helpful in describing how

these systems actually work in the marketplace. The free-market system has been more accurately described by economist Paul Samuelson as a "mixed economy."[22] Mixed economies include a balance between private property systems and the government laws, policies, and regulations that protect consumers and citizens. In mixed economies, ethics becomes part of legal and business debates. Principles of justice, rights, and duty coexist with utilitarian and market principles.

A realistic approach to managing social responsibility in a mixed-market economy is the stakeholder management approach. Instead of separating profit-making from social and ethical goals, corporate leaders can accomplish both, as the following sections show.

POINT/COUNTERPOINT

Too Big to Fail (TBTF)

The "theory" behind "too big to fail" (TBTF) institutions was invoked during the most recent U.S. financial crisis. Governmental assistance to large failing financial institutions, mainly some of the largest banks, was necessary because their failure would have been catastrophic for the U.S. and even global economies. The idea was and is unpopular in part because it justifies subsidizing the Wall Street institutions that played a significant part in that near meltdown. Since banks and these larger financial institutions are returning to their previous practices, the next major meltdown may be closer than previously believed possible.

On the other hand, some progress has been made. The Federal Deposit Insurance Corp. claims it is now prepared to take over the parent companies of large failing lenders, if necessary. Making banks safer for the economy means opening more capital to facilitate investments and loans. Banks have to be able to invest to survive and thrive. The financial health of the four TBTF banks (Bank of America, Citigroup, JPMorgan, Wells Fargo) is central to the U.S. economy as this country faces the continued debate on the debt ceiling and the failed monetary policy that will soon be led by the new Federal Reserve chairperson. The larger a firm's capital is at any time, the larger the shrinkage in asset values it can suffer before becoming insolvent. It seems obvious that the purpose of helping a large bank and financial institution gain safety and protection from failure is to raise its capital requirements, so it can take any shock to the value of its assets.

But again, TBTF helps large banks at the expense of community banks, which are also essential to our economy, small investors, and individuals. By making failure less common, it creates "moral hazard" (the subsidization of bad behavior) in our financial system. To avoid another 2008 near meltdown, a robust plan to take over a failing financial firm is needed, and market participants need to understand that they have to absorb their own losses—not taxpayers. Investors have to believe that banks are "too big to bail." On the other hand, shareholders, creditors, and the parent company would have to take the pain—even to the point of going out of business. Shareholders would

be out of business, creditors would sustain huge losses, and top executives probably would be fired.

Instructions: (1) Each student individually adopts *either* the Point *or* CounterPoint argument below, justifying their reasons (using arguments from this case and other evidence/opinions). (2) Then, either in teams or designated arrangements, each shares their reasons. (3) Class debrief and sharing of insights.

POINT: Let them fail if they bring it on themselves and everybody else. Wall Street titans, risky bankers, and investors who seek only financial gain have forgotten the original mission of banks and financial investment firms: to help small businesses, individual investors, and families needing mortgages to get those funds. This is what growing and sustaining a middle class, a democratic society, and a socially responsible business environment is all about; the U.S. stock market and business system is based on honest yet "competitive enough" strategies and practices.

COUNTERPOINT: Large financial institutions and banks must be supported to compete with global rivals and to protect the U.S. standard of living and way of life. Such institutions are large but require support.

It is naive to believe that small banks and financial institutions can finance multimillion-dollar real estate and other projects that support the economic and social growth that sustains the standard of living of Americans and other global citizens. Enabling banks to grow capital to protect their assets during downtimes is one of the only ways to permit them to survive; otherwise, the government and taxpayer dollars will be needed. The United States is not a socialist or government-run society, rather it is based on free enterprise where there are no artificial ceilings for growth.

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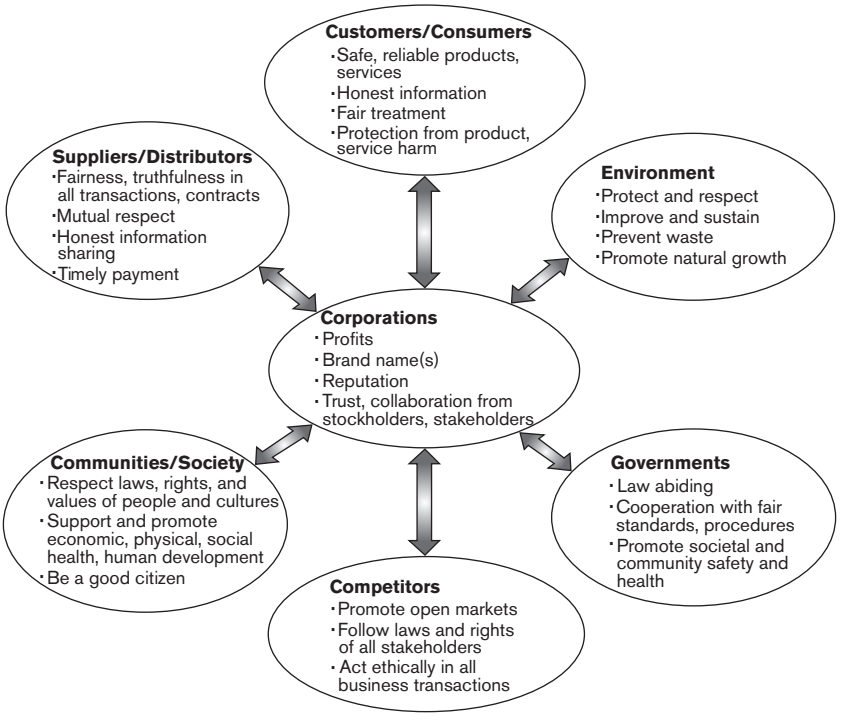
4.2 Managing Corporate Responsibility with External Stakeholders

The Corporation as Social and Economic Stakeholder

The stakeholder management approach views the corporation as a legal entity and also as a collective of individuals and groups. The CEO and top-level managers are hired to maximize profits for the owners and shareholders. The board of directors is responsible for overseeing the direction, strategy, and accountability of the officers and the firm. To accomplish this, corporations must respond to a variety of stakeholders' needs, rights, and legitimate demands. From this perspective, the corporation has primary obligations to the economic mandates of its owners; however, to survive and succeed, it must also respond to legal, social, political, and environmental claims from stakeholders, as noted earlier. Figure 4.1 illustrates the moral stakes and corporate responsibilities of firms' obligations toward their different stakeholders.

Figure 4.1

External Stakeholders, Moral Stakes, and Corporate Responsibilities



Source: Based on Caux Round Table. (March 2009; updated May 2010). Principles for business. *CauxRoundTable.org.* http://www.cauxroundtable.org/index.cfm?menuid=8, accessed January 10, 2014.

One study has argued that "Using corporate resources for social issues not related to primary stakeholders may not create value for shareholders."[23] This finding does not suggest that corporations refrain from philanthropic activities; rather, "The emphasis on shareholder value creation today should not be construed as coming at the expense of the interests of other primary stakeholders."[24]

Shareholder value obsession began in 1976, when it was argued that the owners of companies were not getting full, open, and honest disclosure from professional managers.[25] A major problem was and is not with placing the emphasis on "shareholder value," but on "the use of short-term increases in a firm's share price as a proxy for it." "Ironically, shareholders themselves have helped spread this confusion. Along with activist hedge funds, many institutional investors have idolized short-term profits and share-price increases rather than engaging recalcitrant managers in discussions about corporate governance or executive pay. Giving shareholders more power to influence management (especially in America) and encouraging them to use it should prompt them and the managers they employ to take a longer view."[26]

Critics have not identified a realistic alternative measure of success to shareholder value. Critics of the shareholder model endorse a "stakeholder" model as described and used in this text. [27] "For capitalism to thrive, it urgently needs reform in three areas: shifting from a narrow focus on shareholders to a broader community of stakeholders; adopting an owner-based governance model aimed at building companies with high longevity; and moving from quarterly measures of performance to much longer timeframes."[28]

Corporations are economic *and* social stakeholders. This is not a contradiction but a leadership awareness and choice that requires balancing economic and moral priorities. In the discussion below, we explore the ethical basis on which the relationships between corporations and their stakeholders are grounded. We then turn to the external compliance and legal dimension of stakeholder management, which is also required for effectively dealing with external constituencies.

The Social Contract: Dead or Desperately Needed?

The stakeholder management approach of the corporation is grounded in the concept of a social contract. Developed by early political philosophers, a social contract is a set of rules and assumptions about behavior patterns among the various elements of society. Much of the social contract is embedded in the customs of society. Some of the "contract provisions" result from practices between parties. Like a legal contract, the social contract often involves a quid pro quo (something for something) exchange. Although globalization, massive downsizing, and related corporate practices continue to pressure many employer–employee relationships, the underlying principles of the social contract, like mutual trust and collaboration, remain essential. Reputation of a firm, as well as for leaders, managers and professionals, is still a foundation for business as well as social exchanges, contracts, and practices.

The social contract between a corporation and its stakeholders is often based on implicit as well as explicit agreements. For example, as Figure 4.1 indicates, when corporations and stakeholders base their negotiations and provisions of services and products on moral standards as well as production-oriented metrics, the success of the business and the satisfaction of the stakeholders increase, and the public's confidence in the businesses also is enhanced. A loss of public confidence can be detrimental to the firm and to its investors. One way to retain and to reinforce public confidence is by acting in an ethical manner, a manner that shows a concern for the investing public and the customers of the firm.[29] The question is not really whether a social contract between a corporation and its stakeholders exists, but what the nature of the contract is and whether all parties are satisfied with it. Are customers satisfied with the products and services and how they are treated by a company's representatives? Are suppliers, distributors, and vendors all satisfied by the contractual agreements with the corporation? Do members of the communities a company is located in and serves believe the company is a responsible and responsive citizen? Does the company pay its fair share of taxes? Do employees believe they are paid a fair wage, have adequate working conditions, and are being developed?

Balance between Ethical Motivation and Compliance

Ethics programs, as part of the social contract, are essential motivators in organizations. Studies suggest that ethics programs matter more than compliance programs on several dimensions of ethics, for example, awareness of issues, search for advice, reporting violations, decision making, and commitment to the firm.[30] Business relationships based on mutual trust and ethical principles combined with regulation result in long-term economic gains for organizations, shareholders, and stakeholders.[31] If corporate leaders and their firms commit illegal acts, taxpayers end up paying these costs. Corporate leaders and their stakeholders, therefore, have an interest in supporting their implicit social contract as well as their legally binding obligations.

There is a balance to be maintained between external regulation and self-regulation based on the public's trust in corporations. A 2011 Maritz poll found that "approximately 25% of employees report having less trust in management than they did last year. Only 10 percent of employees trust management to make the right decision in times of uncertainty. The percentage increases to 16% among employees 18–24 years of age who only recently entered the workforce and didn't directly experience many of the management scandals of the past 10 years." The poll also notes that only "slightly more than one in ten Americans (14%) believes their company's leaders are ethical and honest. In addition, the poll found that only 12% of employees believe their employer genuinely listens to and cares about its employees, and only seven percent of employees believe senior management's actions are completely consistent with their words."[32] This mistrust has translated into a global call for greater regulation of large companies. A poll of 20 nations found that "solid majorities in every country favored more regulation of large companies to protect the

rights of workers, the rights of consumers, and the environment. A majority in 15 of the 20 countries also favored greater government regulation to protect the rights of investors."[33]

Covenantal Ethic

The covenantal ethic concept is related to the social contract and is also central to a stakeholder management approach. The covenantal ethic focuses on the importance of relationships—social as well as economic—between businesses, customers, and stakeholders. Relationships and social contracts (or covenants) between corporate managers and customers embody a "seller must care" attitude, not only "buyer beware."[34] A manager's understanding of problems is measured not only over the short term, in view of concrete products, specific cost reductions, or even balance sheets (though obviously important to a company's results), but also over the long term, in view of the quality of relationships that are created and sustained by business activity.[35] It may also be helpful to understand the concept of a covenantal ethic in an organizational context by pointing out how great leaders are able to attract and mobilize followers to a vision and beliefs based on the relationship they develop with those being led. Classic leaders like Franklin Roosevelt, John F. Kennedy, and Martin Luther King Jr. instilled an enduring trust and credibility with their followers. We explain more of these dynamics in Chapter 6; here, the point is that corporate leaders still inspire and motivate followers through their vision, purposive mission, and leading-by-example that result in a type of social contract. Warren Buffet, Bill Gates, and Richard Branson are such examples.

The Moral Basis and Social Power of Corporations as Stakeholders

Keith Davis argues that the social responsibility of corporations is based on social power, and that "if a business has the power, then a just relationship demands that business also bear responsibility for its actions in these areas." He terms this view the "iron law of responsibility" and maintains that "in the long run, those who do not use power in a manner in which society considers responsible will tend to lose it." Davis discusses five broad guidelines or obligations business professionals should follow to be socially responsible:

1. Businesses have a social role of "trustee for society's resources." Since society entrusts businesses with its resources, businesses must wisely serve the interests of all their stakeholders, not just those of owners, consumers, or labor.
2. Business shall operate as a two-way open system with open receipt of inputs from society and open disclosure of its operations to the public.
3. "Social costs as well as benefits of an activity, product, or service shall be thoroughly calculated and considered in order to decide whether to proceed with it." Technical and economic criteria must be supplemented with the social effects of business activities, goods, or services before a company proceeds.

4. The social costs of each activity, product, or service shall be priced into it so that the consumer (user) pays for the effects of his consumption on society.
5. Business institutions as citizens have responsibilities for social involvement in areas of their competence where major social needs exist.[36]

The above guidelines provide a foundation for creating and reviewing the moral bases of corporate stakeholder relationships. The public is intolerant of corporations that abuse this mutual trust, as recent surveys show. For example, a BusinessWeek/Harris Poll found that "72% of Americans say they believe that business has too much power over American life. Furthermore, 66% of those polled agree that companies care more about making large profits than about selling safe, reliable, quality products. At the same time, pressure for companies to take on more responsibilities in their communities seems to be rising."[37]

The MSN Money Customer Service Hall of Fame includes the 10 companies out of 150 of the country's largest consumer names most often rated as "excellent" for customer service in MSN Money's survey. In 2013, they were Amazon.com, Marriott, Hilton, UPS, FedEx, Google, State Farm, Samsung, Trader Joe's and Lowe's. Among the ten worst companies for customer service in 2013 were financial institutions and cable and insurance providers: Bank of America (bank), Comcast, Bank of America (credit card), Dish Network, Citigroup (credit card), Wells Fargo (credit card), Wells Fargo (bank), Citibank (bank), AT&T, and Discover Financial Services. Whereas economic, environmental, and other factors affect customer satisfaction with companies and industries—especially those listed in this survey at this time—if an industry or company continues to score low on the index, it should serve as a wakeup call to the stockholders and corporate leaders. Many times some element of poor stakeholder management can also be part of the problem, whether perceived or experienced.[38]

Corporate Philanthropy

Corporations practice social responsibility in several ways, also known as "external engagements," which means the efforts a company makes to manage its relationships with stakeholders and groups and institutions in need of assistance. These relationships can and should include a wide variety of activities: not just corporate philanthropy, community programs, and political lobbying, but also aspects of product design, recruiting policy, and project execution. "In practice, however, most companies have relied on three tools for external engagement: a full-time CSR team in the head office, some high-profile (but relatively cheap) initiatives, and a glossy annual review of progress."[39]

Such activities are often measured through the impact of corporate philanthropy by counting the number of individuals who are helped by a particular program. Philanthropy, however, can also reduce business risk, open up new markets, engage employees, build the brand, reduce costs, advance technology, and deliver competitive returns. "Corporate philanthropy is usually

defined in contrast to various 'shared' or 'blended' value approaches to corporate social responsibility (CSR), in which companies seek to do well by doing good." It is more helpful to view corporate philanthropy as a discovery phase in investment in a social issue. Such philanthropic investments can serve as incubators for promising ideas and mechanisms for learning both community and corporate needs. "Much like R&D, philanthropy allows companies to make thoughtful investments in sectors where the return profile is typically more speculative. Of course, philanthropy is not the only strategy for companies to play meaningful corporate-citizenship roles. Business leaders should use every tool in their CSR portfolio to help create economic value that can help address relevant societal issues."[40]

A corporation's social responsibility also includes certain types of philanthropic responsibilities, in addition to its economic, legal, and ethical obligations. Corporate philanthropy is an important part of a company's role as "good citizen" at the global, national, and local levels. The public expects, but does not require, corporations to contribute and "give back" to the communities that support their operations. Procter & Gamble's reputation has been enhanced by its global contributions. Some of the greatest recent corporate philanthropists include Warren Buffet, Bill and Melinda Gates, and Mark Zuckerberg.[41] Buffett pledged 12,220,852 shares of Berkshire Hathaway class "B" stock, valued at more than $1 billion, to each of his three children's foundations. The Howard G. Buffett Foundation has contributed funds to agricultural development, clean-water projects, and programs working to fight poverty.[42]

Managing Stakeholders Profitably and Responsibly: Reputation Counts

Globalization and the shifting centers of financial power and influence, the ongoing diffusion of information technology, and the threat of other Enrons continue to pressure corporate competition, along with increasingly wider shareholder activism. "The result is that many employees, investors, and consumers are seeking assurances that the goods and services they are producing, financing, or purchasing are not damaging to workers, the environment, or communities by whom and where they are made."[43] There is, consequently, renewed interest in the area of CSR; that is, how a business respects and responds responsibly to its stakeholders and society as well as to its stockholders.[44]

Ethical Insight 4.2

Employers' Agreed on Goals for Colleges and Universities

A recent online survey by Hart Research Associates showed that employers place the greatest degree of importance on the following areas:

- *Ethics:* "Demonstrate ethical judgment and integrity" (96% important; 76% very important).

- *Intercultural Skills:* "Comfortable working with colleagues, customers, and/or clients from diverse cultural backgrounds" (96% important, 63% very important).
- *Professional Development:* "Demonstrate the capacity for professional development and continued new learning" (94% important, 61% very important).

Questions for Discussion

1. Do you agree that college/university education should emphasize ethical judgment and integrity as a priority in learning? Why or why not?
2. If so, do you believe learning ethical judgment and integrity are as important as the major one chooses as a concentration? Explain.

Source: Hart Research Associates. (April 13, 2013). It takes more than a major: Employer priorities for college learning and student success, an online survey among employers conducted on behalf of: the Association of American Colleges and Universities, p. 6 (4th area of online survey out of 11). *AACU.org.* http://www.aacu.org/leap/documents/2013_EmployerSurvey.pdf, accessed January 8, 2014.

Most executives and professionals are interested in their stakeholders and are law abiding. Reputation remains one of the most powerful assets in determining the extent to which a company manages its stakeholders effectively. There is also evidence that socially responsible corporations have a competitive advantage in the following areas:

1. Reputation.[45]
2. Successful social investment portfolios.[46]
3. Ability to attract quality employees.[47]

The organization Business Ethics ranks the top 100 socially responsible corporations in terms of citizenship. Business Ethics uses its own collected data, including the Domini 400 Social Index (which also tracks, measures, and publishes information on companies that act socially responsible). The Standard & Poor's 500 plus 150 publicly owned companies are ranked on a scale that measures stakeholder ratings. Harris Interactive, Inc. and Reputation Institute, a New York–based research group, conducted an online nationwide survey of 10,830 people to identify the companies with the best corporate reputations among Americans at the turn of the millennium.[48] The Reputation Quotient (RQ) is a standardized instrument that measures a company's reputation by examining how the public perceives companies based on 20 positive attributes, including emotional appeal; social responsibility; good citizenship in its dealings with communities, employees, and the environment; the quality, innovation, value, and reliability of its products and services; how well the company is managed; how much the company demonstrates a clear vision and strong leadership; and profitability, prospects, and risk.

The executive director of the Reputation Institute, Anthony Johndrow, noted, "Reputation is much more than an abstract concept; it's a corporate

asset that is a magnet to attract customers, employees, and investors."[49] Google took top place in the Reputation Institute's annual Global Pulse U.S. 2011 study, with Apple and The Walt Disney Company following at second and third place. The study measures an "analysis of the world's 100 top-rated companies based on input from over 55,000 consumers in 15 countries." The following trends were discovered as a result of this study:

- "58% of people's willingness to recommend a company is driven by their perception of the company; only 42% depends on perceptions of the company's products and services.
- Two-thirds of C-suite executives at the 150 largest U.S. companies believe we have already entered the Reputation Economy.
- Among the 150 largest companies in the U.S., 25 percent now coordinate their reputation strategy and enterprise story through the CEO's office.
- Companies with excellent reputations are two and a half times more likely to have CEOs setting the strategy for enterprise positioning than those with weaker reputations."[50]

Brands are among companies' most—if not *the* most—valued assets because they reflect and are an integral part of their reputations and identities. The top ten most and least reputable brands in America for 2013 are listed in Table 4.1.

Table 4.1
Ten Most- and Least-Reputable Companies in America (2013)

Ten most-reputable brands	Ten least-reputable brands
1. Amazon	51. Comcast
2. Apple	52. Wells Fargo
3. Walt Disney	53. JPMorgan Chase
4. Google	54. BP
5. Johnson & Johnson	55. Citigroup
6. Coca-Cola	56. Bank of America
7. Whole Foods Market	57. American Airlines
8. Sony	58. Halliburton
9. Procter & Gamble	59. Goldman Sachs
10. Costco	60. AIG

Source: Ragan's PR Daily. (February 14, 2013). The 10 most– and the 10 least–reputable brands. *PRDaily.com.* http://www.prdaily.com/Main/Articles/The_10_mostand_the_10_leastreputable_bran,13835.aspx#, accessed January 9, 2014. Permission granted; also found in the original source, Harris Interactive. (February 2013). The Harris Poll 2013 RQ® Summary Report, p. 9. For a more complete description of this ranking, see A Survey of the U.S. General Public Using the Reputation Quotient®. http://www.harrisinteractive.com/vault/2013%20RQ%20Summary%20Report%20FINAL.pdf, accessed February 7, 2014.

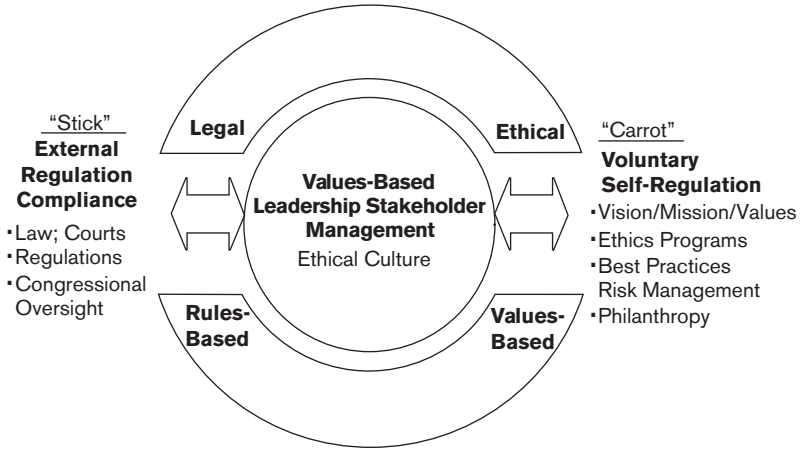
The Harris Poll RQ ranks companies' reputations on six dimensions: social responsibility; vision and leadership; emotional appeal; products and services; financial performance; and workplace environment. The general public rates companies by completing online surveys that are analyzed and used in marketing and policy decisions. You can score your own organization's reputation in Ethical Insight 4.3, "Rank Your Organization's Reputation."

4.3 Managing and Balancing Corporate Governance, Compliance, and Regulation

While leaders and their teams build the reputations of their corporations through high productivity, trust, and good deeds shown toward their stakeholders while satisfying competitive demands of the marketplace, it is also true that laws and regulations set standards for acceptable and unacceptable business practices and behaviors. Just as the market is not entirely "free," neither are all stakeholders and constituencies honest, fair, and just in their motives and business transactions. The corporate scandals exemplified by Enron and others demonstrated that entire corporations can be brought down by top-level executives and their teams. Lessons from the scandals also showed that corporate boards of directors, CEOs, chief financial officers (CFOs), and other top-level administrators require legal constraints, compliance rules, regulation, and the threat and provision of punishment when crimes are committed. Wrongdoers inside and outside corporations must have boundaries set and disciplinary actions applied not only to protect the innocent, but also to enable businesses to exist and succeed. The "rule of law" enables capitalism and

Figure 4.2

Corporate Social Responsibility and Stakeholder Management: Balancing the "Carrot" and "Stick" Approaches



democracies to thrive. Research also shows that both "carrot" (motivational, ethical incentives) and "stick" (legal compliance and potential disciplinary action) approaches are necessary to enable workforces and leaders to be productive and law-abiding. Figure 4.2 illustrates a "carrot and stick" balancing approach that effective corporations use in providing both a legal and ethical culture and transactions, internally and with external stakeholders, as shown in Figure 4.2.

Ethical Insight 4.3

Rank Your Organization's Reputation

Score a company, college, or university at which you worked or studied on the following characteristics. Be objective. Answer each question based on your experience and what you objectively know about the company, college, or university.

1 = very low; 2 = somewhat low; 3 = average; 4 = very good; 5 = excellent

___ Emotional appeal of the organization for me

___ The social responsibility of the organization

___ The organization's treatment of employees, community, and environment

___ The quality, innovation, value, and reliability of the organization's products and/or services

___ The clarity of vision and strength of the organization's leadership

___ The organization's profitability, prospects in its market, and handling of risks

___ Total your score

Interpretation: Consider 30 a perfect score, 24 very good, 18 average, 12 low, and 6 very low.

Questions for Discussion

1. How did your company/organization do on the ranking? Explain.
2. Explain your scoring on each item; that is, give the specific reasons that led you to score your company as you did.
3. Suggest specific actions your organization could take to increase its Reputation Quotient.

In this section, we discuss the "stick" approach (legal compliance and regulation) in more detail. With our focus here on the corporation and external stakeholders, we limit our discussion of laws to (1) the Sarbanes-Oxley Act (SOX), and a brief overview of the (2) Federal Sentencing Guidelines for Organizations (FSGO), and then discuss (3) laws regulating competition, consumer protection, employment discrimination/pay/safety, and the environment. Chapter 5 covers legal and social issues related to the corporation and consumer stakeholders, and Chapter 7 addresses employee stakeholders.

Most corporations effectively govern themselves, to a large extent, through their own control systems and stakeholder relationships. A public corporation's federal and state charter provides the legal basis for its board of directors, stockholders, and officers to govern and operate the company. However, as Enron and other corporate scandals have demonstrated, self-governance cannot be counted on to work well alone. A question often repeated from the scandals is, "Where were the boards of directors when the widespread fraud, deception, and abuse of power occurred?"

A recent *Time* magazine cover read, "How Wall Street Won: Five Years after the Crash, It Could Happen All Over Again."[51] The article makes five recommendations for preventing another financial subprime mortgage lending crisis, based on the author's research and interviews with leading experts from financial and university institutions: 1. Fix the Too-Big-To-Fail Problem, 2. Limit the Leverage (of banks), 3. Expose Weapons of Mass Financial Destruction ("derivatives" trading), 4. Bring Shadow Banking Into the Light, and 5. Reboot the Culture of Finance. In summary, these five recommendations argue that some of the largest banks in the United States need closer self- and government regulation in their lending and investing practices in order to stop certain derivatives and high-risk investing from wrecking the economy again. Steps toward this goal include reinstating the former Fed chairman Paul Volcker's rule to "separate government-insured commercial lending from risky trading operations." Reinstating and implementing provisions of the 1933 Glass-Steagall Act, which separates commercial from risky lending practices by banks, along with the Dodd-Frank legislation, would also address this problem.

Other suggestions include limiting the leverage larger banks and mortgage companies have to make risky loans. Leverage means the ability "to borrow more money than they can immediately repay." Too much leverage gives banks incentives to overinvest more funds than they have to meet their operating obligations. Also, making "shadow banking"—hiding the amount and types of investments made—more transparent would expose those financiers who put banks, customers' money, and the economy at risk. Finally, "rebooting the culture of finance" in the United States is necessary. The United States suffers from the Wall Street-driven "financialization" of the economy. The original purpose and mission of banks is to lend to real people and businesses, not using customers' and small businesses' money to bankroll high-risk investing, especially when the larger banks limit access to credit to small banks and individuals. Also, the credit ranking system of banks that pays professionals in that system to rank them must change. This system is self-defeating; the credit ratings do not change banking practices, and large-scale questionable investment banking practices could lead to further meltdowns of the economy.[52]

There are a number of other reasons why many of the larger, prominent corporate boards of directors in different industries, not only banking, did not execute their mandated legal and ethical responsibilities during the past financial meltdown and crisis. These include lack of independence, insider roles and relationships, conflicts of interest, overlapping memberships of board

members with other boards, decision-by-committees, well-paid members with few responsibilities, and lack of financial expertise and knowledge about how companies really operate.[53] There, however, are improvements being made legislatively and in business and board practices.

Best Corporate Board Governance Practices

Most corporate boards act responsibly toward their stakeholders and in the best interests of shareholders. The wake of the large corporate scandals of the early 2000s has led to several best practices for a board of directors. "The Board of Directors must be committed to its functions, be functional and make informed decisions."[54] This can be achieved through greater objectivity, independence, and oversight by all board members.[55]

> With very few exceptions, governance activists have achieved most of the reforms they have sought to effectuate. According to Spencer Stuart's 2012 U.S. Board Index, 84% of S&P 500 companies have adopted a majority voting standard, 83% have annually elected boards, and 84% of their directors are independent—to name but a few of the more trendy governance issues in recent years. However, those who make their living in the corporate governance industry will undoubtedly continue to push these proposals at smaller companies, and come up with additional requirements and heightened standards to propose with each new proxy season. By way of example, ISS's 2013 corporate governance policy updates tighten its board responsiveness policy and recommend that shareholders vote "against" or "withhold" their votes for incumbent directors who fail to act on a shareholder proposal that received the support of a majority of votes cast in the previous year, as compared to ISS's prior standard, which looked at whether the proposal received a majority of outstanding shares the previous year or the support of a majority of votes cast in both the last year and one of the two prior years.[56]

The following section discusses the two laws best known for defining the regulations and best practices for companies and their boards of directors.

Sarbanes-Oxley Act

The 2002 Sarbanes-Oxley Act (SOX) was a direct regulatory response by Congress to corporate scandals. (PricewaterhouseCoopers called this law the most important legislation affecting corporate governance, financial disclosure, and public accounting practice since the 1930s.)[57] The "carrot" approach, or corporate self-regulation, did not work for Enron and other firms involved in scandals; Congress realized that a "stick" approach (laws, regulations, disciplinary actions) was also required. A summary of SOX shows that federal provisions were established to provide oversight, accountability, and enforcement of truthful and accurate financial reporting in public firms. Some of the major issues included (1) a lack of an independent public company accounting board to oversee audits, (2) conflicts of interest in companies serving as

auditors and management consultants to companies, (3) holding top-level officers (CEOs and CFOs) accountable for financial statements, (4) protecting whistle-blowers, (5) requiring ethics codes for financial officers, and (6) other reforms as the list below shows.

The key aspects of SOX can be summarized as follows:

- Establishes an independent public company accounting board to oversee audits of public companies.
- Requires one member of the audit committee to be an expert in finance.
- Requires full disclosure to stockholders of complex financial transactions.
- Requires CEOs and CFOs to certify in writing the validity of their companies' financial statements. If they knowingly certify false statements, they can go to prison for 20 years and be fined $5 million.
- Prohibits accounting firms from offering other services, like consulting, while also performing audits. This constitutes a conflict of interest.
- Requires ethics codes for financial officers of companies that are registered with the Securities and Exchange Commission (SEC).
- Provides a 10-year penalty for wire and mail fraud.
- Requires mutual fund professionals to disclose their vote on shareholder proxies, enabling investors to know how their stocks influence decisions.
- Provides whistle-blower protection for individuals who report wrongful activities to authorities.
- Requires attorneys of companies to disclose wrongdoings to senior officers and to the board of directors, if necessary; attorneys should stop working for the companies if senior managers ignore reports of wrongdoings.[58]

SOX also defines several reforms aimed at improving problems of boards of directors.

There are other "best practices" guidelines for boards, including:

1. Separating the role of chairman of the board when the CEO is also a board member.
2. Setting tenure rules for board members.
3. Regularly evaluating itself and the CEO's performance.
4. Prohibiting directors from serving as consultants to the companies which they serve.
5. Compensating directors with both cash and stock.
6. Prohibiting retired CEOs from continuing board membership.
7. Assigning independent directors to the majority of members who meet periodically without the CEO.[59]

The roles and responsibilities of CEOs and organizational leaders are discussed in Chapter 6.

The July/August 2012 cover story of *Financial Executive* was titled "Sarbanes-Oxley—A Decade Later" and summarized the impact of SOX:

> The act created the Public Company Accounting Oversight Board to police the accounting profession and set auditing standards. It shored up the role of the audit committee, making it independent and responsible for hiring, firing and overseeing external auditors, removing that authority from management.
>
> Under Section 404, companies were required to establish internal controls and procedures for financial reporting. Another section mandated that both the chief executive and chief financial officers personally attest that they have reviewed the auditors' report and that it "does not contain any material with untrue statements or material omission" or anything that could be "considered misleading."
>
> Sarbanes-Oxley also instituted "clawback" provisions requiring CEOs and CFOs to return ill-gotten gains to their employer. In one notable case, Ian McCarthy, former CEO at Atlanta-based Beazer Homes USA Inc., and former CFO James O'Leary both agreed to return all of their cash bonuses, incentive and equity-based compensation for 2006. McCarthy had to relinquish more than $5.7 million in cash plus $772,232 in stock sale profits, along with some 120,000 in restricted stock shares; O'Leary returned $1.4 million.[60]

But Congress has been moving in the opposite direction. Two recent laws—the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and 2013's Jumpstart Our Business Startups Act (the JOBS Act)—have largely served to weaken SOX. Dodd-Frank exempted public companies with a "public float" below $75 million, thereby removing 42% of public companies, according to figures cited by the Council of Institutional Investors and Center for Audit Quality in a joint letter last November.[61] The letter implored both the chairman and ranking members of the House Financial Services Committee to not further reduce safeguards, to no avail. Similarly, a broad range of investor-protection groups and regulators have expressed alarm that the JOBS Act, signed into law by President Barack Obama in early April, "guts" SOX. Among other things, it exempts newly public "emerging growth companies" from meeting Section 404 obligations for five years following an initial public offering.[62]

Pros and Cons of Implementing the Sarbanes-Oxley Act

Critics of SOX argue against the implementation and maintenance of the law for the following reasons:

1. It is too costly. One estimate from a survey by Financial Executives International stated that firms with $5 billion in revenue could expect to spend on average $4.7 million implementing the internal controls required, then $1.5 million annually to maintain compliance.[63] An average first-year cost for complying with Section 404 of the Act (i.e., creating reliable internal financial controls and having management and an independent auditor confirm the reliability) was estimated at $4.36 million.[64] Others argue that the

costs exceed the benefits, especially for small firms. "Smaller companies that are audited by the Big Four will have to pay higher audit fees even if they are not subject to Sarbanes-Oxley as the additional audit requirements of Sarbanes-Oxley creep into their methodologies. Many private companies and smaller public companies are realizing that the Big Four have designed their audits to serve the *Fortune* 500 companies and that this model is slow and expensive."[65]

2. It impacts negatively on a firm's global competitiveness. This argument is also based on the costs of keeping internal operations compliant with the act. Critics argue that other companies around the globe do not have this expense, so why should U.S. public firms?

3. Government costs also increase to regulate the law.

4. CFOs are overburdened and pressured by having to enforce and assume accountability required by the law.

5. Critics claim that implementing SOX requirements throughout an organization is too costly and wasteful for small and mid-sized firms wishing to go public.

6. SOX reduces the willingness of corporations to take risks.

7. Accrual accounting is seen as being more "expensive" under SOX, as certain expenses like R&D must be expensed when incurred, reducing current earnings. This may make earnings management a more attractive and "cheaper" option for management.

8. SOX is sometimes faulted for not preventing the financial crisis and the great recession of 2008–2009, from which the U.S. economy has yet to recover.[66]

Paul Volcker and Arthur Levitt, two widely respected experts previously from the SEC and Federal Reserve respectively, offered the following counterclaims to some of the previous criticisms:[67]

1. The costs of implementing SOX are minimal compared to the costs of not having it—recall the $8 trillion in stock losses alone during the great "recession" and banking crisis of 2008 and the near collapse of the global economy, not counting the damage done to employee families and effects on the economy at large.

2. "Companies have better internal control environments as a result of Sarbanes-Oxley. This will lead to more accurate information being available to investors who are more confident in making investing decisions. All participants in financial reporting have increased responsibilities and consequences for not living up to those responsibilities."[68]

3. The changes required to implement this law are difficult; however, a recent *Corporate Board Member* magazine survey found that more than 60% of 153 directors of corporate boards of directors believe the effect of SOX has been positive for their firms, and that more than 70% viewed the law as also positive for their boards.[69]

4. The data does not support the argument that this law presents a competitive disadvantage to global firms. The NASDAQ stock exchange added

six international listings in the second quarter of 2004. A survey by Broadgate Capital Advisors and the Value Alliance found that only 8% of 143 foreign companies that issue stocks that trade in the United States claimed that SOX would cause them to rethink entering the U.S. market.[70]

5. If a company uses SOX as a reason to not go public, the firm should not go public or use investors' funds. U.S. markets are among the most admired in the world because they are the best regulated.

6. Financial officers who complain about the requirements of SOX may in fact be suffering from the lack of internal controls they had before. In 2003, 57 companies of all sizes said they had material weaknesses in their controls, after their auditors, who were paid to test financial controls, were terminated. These same auditors decreased their testing of internal controls because they faced pressures to cut their fees.

7. Requiring top executives and financial officers to personally sign off on and take personal ownership of the books is an initial deterrent of fraud and improves organizational culture.

8. SOX has resulted in improvements in the accounting industry in the wake of the fall of former accounting giant Arthur Andersen, at the hand of the Public Company Accounting Oversight Board.

9. Ernst & Young's Les Brorsen sees creation of the PCAOB to police the auditing profession—coupled with corporate governance rules' putting a public company's board-level audit committee, rather than company management, in charge of the auditing process—as "the top two fundamental changes" brought about by the act. "It's fair to say that the largest single impact of Sarbanes-Oxley was to end 100 years of self-regulation," he says. Related to that, Brorsen adds, "Improved corporate governance is one of the hallmarks of the legislation."[71]

The costs and benefits of implementing SOX continue to be debated. Still, Volcker and Levitt argue that, "While there are direct money costs involved in compliance, we believe that an investment in good corporate governance, professional integrity, and transparency will pay dividends in the form of investor confidence, more efficient markets, and more market participation for years to come."[72] Certainly guidelines and specific ways to simplify, decrease unnecessary costs, and streamline implementation of this law must be addressed as companies strive to compete locally, nationally, and especially globally.

The Federal Sentencing Guidelines for Organizations: Compliance Incentive

Before the 2002 SOX, the 1991 Federal Sentencing Guidelines for Organizations (FSGO) were passed to help federal judges set and mitigate sentences and fines in companies that had a few "bad apples" who had committed serious crimes. The FSGO were also designed to alleviate sentences on companies that had ethics and compliance programs. Under the FSGO, a corporation (large or small) receives a lighter sentence and/or fine—or perhaps no sentence or probation—if convicted of a federal crime, provided that the firm's

ethics and compliance programs were judged to be "effective." The FSGO changed the view of corporations as entities that were legally liable and punishable for criminal acts committed within their boundaries to the view of the corporation as a moral agent responsible for the behavior of its employees. As a moral agent, the corporation could be evaluated and judged on how effective the leaders, culture, and ethics training programs were toward preventing misconduct and crime.[73]

Companies that acted to prevent unethical and criminal acts would, under the FSGO, be given special consideration by judges when being fined or sentenced. A points system was established to help mitigate the fine and/or sentence if the company displayed the following seven criteria:

1. Established standards and procedures capable of reducing the chances of criminal conduct.
2. Appointed compliance officer(s) to oversee plans.
3. Took due care not to delegate substantial discretionary authority to individuals who are likely to engage in criminal conduct.
4. Established steps to effectively communicate the organization's standards and procedures to all employees.
5. Took steps to ensure compliance through monitoring and auditing.
6. Employed consistent disciplinary mechanisms.
7. When an offense was detected, took steps to prevent future offenses, including modifying the compliance plan, if appropriate.[74]

The FSGO have been revised to reflect the post-Enron corporate environment. The revisions add specificity to the 1991 version, include top-level officers' accountability, and attempt to increase the effectiveness and integration of a company's ethics and compliance programs with its culture and operations. Ed Petry, former director of the Ethics Officer Association (EOA), served on the federal committee that revised the FSGO. Petry summarized some of the prominent revisions as follows:[75]

- Compliance and ethics programs (C&EP) are now described in a standalone guideline.
- The connection between effective compliance and ethical conduct is stressed.
- Organizations are required to "promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law."

In 2010, the FSGO were revised again. The most notable change promoted the practice of opening a direct line of communication from the chief compliance officer, or those with "operational responsibility for the compliance and ethics program," directly to the governing body on any concerns involving actual or potential criminal conduct.[76] SOX and the Revised Federal Sentencing Guidelines (RFSGO) serve as constraints and deterrents to immoral and criminal corporate conduct that ultimately affects stakeholders and stockholders.

Table 4.2 shows RFSGO. SOX is an attempt by the U.S. federal government to provide stricter compliance guidelines and disciplinary actions to corporations in the wake of corporate scandals. The RFSGO add incentives to companies to self-regulate while following laws aimed at protecting the interests of shareholders and stakeholders, including the public. In the following section, an overview of the role laws and congressional agen-

Table 4.2
Revised Federal Sentencing Guidelines for Organizations (RFSGO) (2004)

1. Exercise due diligence to prevent and detect criminal conduct.

2. Promote an **organizational culture** that encourages ethical conduct and a commitment to compliance with the law.

3. The organization shall use reasonable efforts **not to include within the substantial authority personnel** of the organization **any individual whom the organization knew**, or should have known through the exercise of due diligence, **has engaged in illegal activities** or other conduct **inconsistent with an effective compliance and ethics program.**

4. (A) The organization shall take reasonable steps to **communicate periodically and in a practical manner its standards and procedures,** and other aspects of the compliance and ethics program, to the individuals referred to in subdivision (B) by **conducting effective training programs** and otherwise **disseminating information appropriate to such individuals' respective roles and responsibilities.**
(B) The individuals referred to in subdivision (A) are the members of the governing authority, high-level personnel, substantial authority personnel, the organization's employees, and, as appropriate, the organization's agents.

5. The organization shall take reasonable steps:
(A) to ensure that the organization's compliance and ethics program is followed, including monitoring and auditing to detect criminal conduct;
(B) to evaluate periodically the effectiveness of the organization's compliance and ethics program;
(C) to have and **publicize a system,** which may include mechanisms that **allow for anonymity or confidentiality,** whereby the **organization's employees and agents** may report or seek guidance regarding potential or actual criminal conduct without fear of retaliation.

6. The **organization's compliance and ethics program shall be promoted and enforced consistently throughout the organization** through (A) appropriate incentives to perform in accordance with the compliance and ethics program; and (B) appropriate disciplinary measures for engaging in criminal conduct and for failing to take reasonable steps to prevent or detect criminal conduct.

7. After criminal conduct has been detected, the organization shall take reasonable steps to respond appropriately to the criminal conduct and to prevent further similar criminal conduct, including making any necessary modifications to the organization's compliance and ethics program.

Source: 2004 Federal Sentencing Guidelines, chapter 8, part B: Remedying harm from criminal conduct, and effective compliance and ethics programs excerpted from §8B2.1. Effective Compliance and Ethics Program of the 2004 Federal Sentencing Guidelines. http://www.ussc.gov/Guidelines/2004_guidelines/Manual/gl2004.pdf.

cies play in protecting the public, consumers, and other stakeholders is provided.

4.4 The Role of Law and Regulatory Agencies and Corporate Compliance

Government at the federal, state, and local levels also regulates corporations through laws, administrative procedures, enforcement agencies, and courts. Regulation by the government is necessary in part because of failures in the free-market system discussed earlier. There are also power imbalances between corporations, individual consumers, and citizens. Individual citizens and groups in society need a higher authority to represent and protect their interests and the public good.[77]

The role of laws and the legal regulatory system governing business serves five purposes:

1. Regulate competition.
2. Protect consumers.
3. Promote equity and safety.
4. Protect the natural environment.
5. Ethics and compliance programs to deter and provide for enforcement against misconduct.[78]

The corporate scandals again exemplified a failure of internal corporate governance and self-regulation by all parties (internal and external to corporations) involved. Individual leaders' greed, ineffective boards, investment banks, and financial companies and traders all conspired with Enron and other companies in the scandals to commit fraud, theft, and deceit. Corporate scandals cannot be initiated and sustained without the direct or indirect assistance and/or negligence from the SEC, banks, investment traders and managers, media, Wall Street, federal legislators, and other players.[79] The subprime lending crisis also showed how an entire system of stakeholders in the financial, banking, credit and lending system, and government can be involved in a crisis that has been attributed in large part to "predatory lending" practices. As with the corporate scandals, in the subprime crisis one asks, "Where were the federal, state, and local governmental and congressional regulators?" Still, the justice system did serve sentences to executives in the corporate scandals. Starting with Enron and followed by WorldCom, Qwest, Tyco, HealthSouth, and others, more than $7 trillion in stock market losses were accrued. These losses also cost American employees and families more than 30% of their retirement savings.[80] A quick summary will illustrate the aftermath of some of the major scandals.

- *Enron Corporation:* Former chairman and CEO Ken Lay died before being tried and sentenced. Jeffrey Skilling, a former executive, was fined

$45 million and is currently serving a 24-year, 4-month prison sentence at the Federal Correctional Institution in Waseca, Minnesota.[81] On June 21, 2013, Skilling succeeded in getting his prison sentence reduced by 10 years as part of a court-ordered reduction. With court action, victims of Skilling's crimes will finally receive more than $40 million that he owes them.[82] The former CFO, Andrew Fastow, is currently serving a six-year prison sentence at the Federal Detention Center in Oakdale, Louisiana. His wife, former Enron assistant treasurer Lea Fastow, was sentenced to one year in federal prison and one year of supervised release in a halfway house.[83] Since leaving prison in 2011 and resuming life with his wife Lea and two sons in Houston, where Enron was based, Fastow has kept a low profile. He reportedly now works 9-to-5 as a document-review clerk at the law firm that represented him in civil litigation.[84]

- *WorldCom, Inc.:* Former CEO Bernard Ebbers pleaded not guilty to fraud and conspiracy charges for allegedly leading an accounting fraud estimated at more than $11 billion. A 2002 class action civil lawsuit against Ebbers and other defendants resulted in a settlement worth over $6 billion to be distributed to over 830,000 individuals. Ebbers is currently serving 25 years at a federal prison in Louisiana.[85] Scott Sullivan, former CFO, pleaded guilty to fraud charges, testified against Ebbers, and received a five-year prison sentence. Sullivan is currently serving his sentence at the federal prison in Jessup, Georgia.[86]

- *Tyco International Ltd.:* Former CEO Dennis Kozlowski and CFO Mark Swartz were accused of stealing $600 million from the company. A New York state judge declared a mistrial in the case because of pressure on a jury member. Kozlowski received a sentence of 8 1/3 to 25 years in prison. Both Kozlowski and Swartz could be eligible for parole after six years, 11 months. Kozlowski is currently serving at least eight years and four months at the Mid-State Correctional Facility in Marcy, New York. Swartz was sentenced to at least eight years and four months of prison and ordered to pay $72 million in fines and restitution.[87] On September 23, 2013, both men left a minimum-security prison in Harlem for steady clerical jobs and overnights in apartments following their headline-grabbing $134 million corporate fraud convictions.[88]

- *Adelphia Communications Corporation:* Founder John Rigas was convicted and sentenced to 12 years. At age 88, Rigas could be a poster child for inmates who might seek early release from prison because of the hazards of advanced aging. His son Timothy received 17 years for conspiracy and bank and securities fraud. Rigas's other son Michael was acquitted of conspiracy charges.[89]

- *Credit Suisse First Boston:* Frank Quattrone, a former investment banking executive who made millions helping Internet companies go public during the dot-com boom, was convicted of obstruction of justice and sentenced to 18 months. His first trial in 2003 ended in a hung jury. Quattrone

now runs Qatalyst Partners, a San Francisco-based investment bank focused on advising technology companies on mergers and acquisitions. The University of Pennsylvania has received a $15 million gift to examine the U.S. criminal justice system from someone who has had some experience with it: Quattrone himself. The justice center will be housed at the law school of the Ivy League university in Philadelphia.[90]

- *HealthSouth Corporation:* Former CEO Richard Scrushy was federally charged with leading a multibillion-dollar scheme that inflated HealthSouth earnings to show the company was meeting Wall Street forecasts. Sixteen former HealthSouth executives were charged as part of a conspiracy to inflate company earnings. Scrushy is the only executive who has not pleaded guilty and is not cooperating with investigators. Scrushy was acquitted in a federal criminal trial related to the alleged $2.7 billion fraud. At a civil trial in Jefferson County Circuit Court in 2009, however, Scrushy was found liable for the accounting fraud and ordered to pay HealthSouth nearly $2.9 billion in damages. In an unrelated case, in 2006 Scrushy and former Alabama governor Don Siegelman were convicted of bribery and honest services fraud. Prosecutors alleged Scrushy bought a seat on a hospital regulatory board by arranging $500,000 in donations to Siegelman's 1999 campaign to establish a state lottery. Scrushy, who was released from prison in 2012, recently lost the appeal of that conviction to the 11th Circuit Court of Appeals. HealthSouth asserts Scrushy has not paid his debt to the company and its shareholders because he owes them $2.8 billion, not counting the rapidly mounting daily interest, according to Scrushy's filing.[91]
- Martha Stewart, founder of Martha Stewart Living Omnimedia, was convicted of conspiracy, obstruction of justice, and lying about her personal sale of ImClone Systems shares. She was refused a new trial on perjury charges against a government witness. Stewart was sentenced to five months in prison. Her broker, Peter Bacanovic, was fined $2,000.[92]
- Samuel D. Waksal, founder and former CEO of ImClone Systems, was sentenced to seven years in prison for securities fraud, perjury, and other crimes he committed with ImClone stock trades to himself, his father, and his daughter at the end of 2001. Waksal founded Kadmon in 2010 as the successor to ImClone, the company that developed the cancer drug Erbitux and was acquired by Indianapolis-based Lilly in 2008. His new company is also working on cancer medicines, and drugs for hepatitis C, inflammatory disorders, and genetic diseases. It's in the same building, along Manhattan's East River, as ImClone. Despite the well-known travails, ImClone was able to bring a very successful drug to market and then get itself acquired. By Wall Street standards, that's a success.[93]
- *Qwest Communications International, Inc.:* Denver federal prosecutors did not win a conviction against four former mid-level executives accused of scheming to deceptively book $34 million in revenue for the company.

Grant Graham, former CFO for Qwest's global business unit; Bryan Treadway, a former assistant controller; Thomas Hall, a former senior vice president; and John Walker, a former vice president, were found not guilty on 11 charges of conspiracy, securities fraud, wire fraud, and making false statements to auditors. Hall received probation and paid a $5,000 fine.[94]

- *American International Group (AIG):* Former vice president Christopher Milton received a four-year sentence in 2009 for his role in a $500 million fraud case. He was convicted of conspiracy, mail fraud, securities fraud, and making false statements to the SEC.[95]
- *Bernard L. Madoff Investment Securities LLC:* In 2009, Bernard Madoff was sentenced to 150 years in prison for his elaborate and long-running Ponzi scheme. Madoff pled guilty to 11 counts of financial crimes.[96]
- *Fannie Mae:* As a result of the Fannie Mae fraud and the subprime mortgage crisis, Leib Pinter, a former executive of Olympia Mortgage Corporation, was sentenced to 97 months in prison on charges of conspiracy to commit wire fraud. He was ordered to pay $43 million in restitution. In December of 2011, the SEC charged six former top executives of Fannie Mae and Freddie Mac with securities fraud.[97]

Why Regulation?

Although governmental legislation and oversight of corporations is an imperfect system, one can always ask: Would you rather live in a system where these laws and controls did not exist? It is also important to note here, as Figure 4.2 shows, that laws are designed to protect and prevent crime and harm, monopolies, and the negative ("externalities") effects of corporate activities (pollution, toxic waste), and also to promote social and economic growth, development, and the health, care and welfare of consumers and the public. Laws provide a baseline, boundaries, and minimum standards for distinguishing acceptable from unacceptable business practices and behaviors. Values, motivations, beliefs, and incentives to do what is right are also necessary in corporations, as they are in other institutions and society in general. The legal and regulatory system is necessary in society and business to establish ground rules and boundaries for transactions. It is not, however, sufficient alone to accomplish this task. The second observation to keep in mind in this discussion is that even with federal, state, and local laws, governmental regulatory agencies in contemporary capitalist democracies are part of political systems—where lobbyists and interest groups compete for resources, influence, and programs for their own ends. In such systems, the legislative and judicial branches of government are designed to provide arbitration and conflict resolution with law enforcement. The following regulatory agencies serve educational as well as legal purposes for corporations serving consumers in the marketplace.

Laws and U.S. Regulatory Agencies

Some of the major laws promoting and prohibiting corporate competition include:

- Sherman Antitrust Act, 1890: Prohibits monopolies, as the case of Microsoft illustrates.
- Clayton Act, 1914: Prohibits price discrimination, exclusivity, activities restricting competition.
- Federal Trade Commission (FTC) Act, 1914: Enforces antitrust laws and activities.
- Consumer Good Pricing Act, 1975: Prohibits price agreements in interstate commerce between manufacturers and resellers.
- Antitrust Improvements Act, 1976: Supports existing antitrust laws and empowers Department of Justice investigative authority.
- FTC Improvements Act, 1980: Empowers the FTC to prohibit unfair industry activities.
- Trademark Counterfeiting Act, 1980: Gives penalties for persons violating counterfeit laws and regulations.
- Digital Millennium Copyright Act, 1998: Protects digital copyrighted material such as music and movies.

Laws Protecting Consumers

Consumers require information and protection from products that may be unsafe, unreliable, and even dangerous, as Chapter 5 shows. While tobacco (now also "smokeless" tobacco), alcohol, and more recently cocaine, along with other so-called dangerous products continue to be marketed, consumer laws and regulatory agencies that you may have seen online or read about have a long history:

- Pure Food and Drug Act, 1906: Prohibits adulteration (ruining) and mislabeling on food and drugs in interstate commerce.
- FTC Act, 1914: Creates the FTC to govern trade and competitive practices.
- Federal Food, Drug, and Cosmetic Act (FDCA), 1938: Amends the Pure Food and Drug Act of 1906 to protect consumers from adulterated and misbranded items and charged the Food and Drug Administration (FDA) with the safety of publically marketed drugs.
- Federal Hazardous Substances Act, 1960: Controls labels on hazardous substances of products used in houses.
- Truth and Lending Act, 1960: Requires full disclosure of credit terms to buyers.
- Consumer Product Safety Act, 1972: Establishes safety standards and regulations of consumer products (created the Consumer Product Safety Commission [CPSC]).
- Fair Credit Billing Act, 1974: Requires accurate, current consumer credit reports.

- Equal Credit Opportunity Act (ECOA), 1974: Prohibits credit discrimination on the basis of race, gender, religion, age, marital status, national origin, or color.
- Fair Debt Collection Practices Act, 1978: Prohibits abusive debt collection practices and allowed consumers to dispute and/or validate debt information.
- Nutrition Labeling and Education Act, 1990: Requires food labels to include standard nutritional facts.
- Telephone Consumer Protection Act, 1991: Issues procedures to avert undesired telephone solicitations.
- Children's Online Privacy Protection Act, 1998: Requires the FTC to make rules to collect online information from children under 13 years old.
- Gramm-Leach-Bliley Act, 1999: Allows commercial banks, investment banks, insurance companies, and securities firms to consolidate.
- Do Not Call Implementation, 2003: Coordinates the FTC and the Federal Communications Commission (FCC) to provide consistent rules on telemarketing practices.
- Fair and Accurate Credit Transactions Act (FACT), 2003: Requires credit agencies to provide a free annual copy of credit reports and created a national system for identity theft fraud alert.

Laws Protecting the Environment

Mercury from China, dust from Africa, smog from Mexico—all of it drifts freely across U.S. borders and contaminates the air millions of Americans breathe, according to recent research from Harvard University, the University of Washington, and many other institutions where scientists are studying air pollution. There are no boundaries in the sky to stop such pollution, no Border Patrol agents to capture it.[98]

The environment is seen less as an inexhaustible free source of clean air, water, soil, and food, and more as a valued resource that requires protection—globally, regionally, and locally. As the sample of environmental laws below indicates, the environment constitutes sources of human, food, vegetation, and animal life.

- Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA), 1947: Regulated the use of pesticides and herbicides. The 1996 amendments facilitate registration of pesticides for special (so-called minor) uses, reauthorize collection of fees to support reregistration, and require coordination of regulations implementing FIFRA and the FDCA.[99]
- Clean Air Act, 1970: Designates air-quality standards; state implementation plans are, however, required for enactment of policies under this Act. In 1990 several progressive and creative new themes were embodied in amendments to the Act, themes necessary for effectively achieving the air-quality goals and regulatory reform expected from these far-reaching amendments.[100] This Act:

  - Encourages the use of market-based principles and other innovative approaches, like performance-based standards and emission banking and trading.
  - Provides a framework from which alternative clean fuels will be used by setting standards in the fleet and California pilot program that can be met by the most cost-effective combination of fuels and technology.
  - Promotes the use of clean low-sulfur coal and natural gas, as well as innovative technologies to clean high-sulfur coal through the acid-rain program.
  - Reduces enough energy waste and creates enough of a market for clean fuels derived from grain and natural gas to cut dependency on oil imports by 1 million barrels/day.
  - Promotes energy conservation through an acid-rain program that gives utilities flexibility to obtain needed emission reductions through programs that encourage customers to conserve energy.
- National Environmental Act, 1970: Establishes policy goals for federal agencies and enacts the Council on Environmental Quality to monitor policies. Amended in 1986.
- Federal Water Pollution Control Act, 1972: Prevents, reduces, and eliminates water pollution. Amended in 1990.
- Marine Protection, Research, and Sanctuaries Act, 1972: Regulated the dumping of materials into the ocean. Amended in 1992.
- Noise Pollution Act, 1972: Controls noise emission of manufactured products.
- Endangered Species Act, 1973: Provides a conservation program for threatened and endangered plants and animals and their habitats.
- Safe Drinking Water Act, 1974: Protects the quality of drinking water in the United States; sets safety standards for water purity and requires owners and operators of public water to comply with standards.
- Toxic Substances Act, 1976: Requires testing of certain chemical substances; restricts use of certain substances. Amended in 1992.
- Oil Pollution Act, 1990: Established penalties for oil spills and damage.
- Food Quality Protection Act, 1996: Requires a new safety standard that must be applied to all pesticides used on foods (reasonable certainty of no harm).

Other laws regarding the environment, consumers, equity and discrimination are discussed in Chapter 7. Taken together, this sample of laws aimed at protecting stakeholders, the public, and the system in which business is conducted indicates the complexity of transactions, responsibilities, and number of stakeholders with which corporations do business. Business ethics and social responsibility can arguably be seen not as a luxury and/or dichotomy, but as a necessity in providing for and protecting the common good. This point should become even more evident in the concluding section of this chapter, which illustrates classic cases of corporate crises in which stakeholder relationships were not well-managed.

4.5 Managing External Issues and Crises: Lessons from the Past (Back to the Future?)

Companies have made serious mistakes as the result of poor self-regulation. As several contemporary corporate crises and now-classic environmental and product- and consumer-related crises illustrate, corporations have responded and reacted slowly and many times insensitively to customers and other stakeholders. The Internet may decrease the time executives have to respond to potential and actual crises.

We conclude this chapter by reviewing some of the major crises from the 1970s to the present, since several of these are only now being resolved. These cases also serve to remind corporate leaders and the public that there is a balance between legal regulation and corporate self-regulation. When corporations fail to regulate themselves and to provide just and fair corrective actions to their failures, government assistance is needed.

We noted in Chapter 3 that issues and crisis management should be part of a company's management strategy and planning process. Failure to effectively anticipate and respond to serious issues that erupt into crises have been as damaging to companies as the crises themselves. Prior to the BP *Deepwater Horizon* oil rig explosion and spill, the *Exxon Valdez* oil spill was biggest U.S. environmental disaster. The Manville Corporation's asbestos crisis is another, almost forgotten disaster, that is also summarized in the feature boxes on the following pages. As the philosopher George Santayana is noted for saying, "Those who do not remember the past are condemned to repeat it." A sample of other classic crises includes the following:

- In June 2001, Katsuhiko Kawasoe, Mitsubishi Motor Company's president, apologized for that firm's 20-year cover-up of consumer safety complaints. (The company also agreed in 1998 to pay $34 million to settle 300 sexual harassment lawsuits filed by women in its Normal, Illinois, plant. This is one of the largest sexual-harassment settlements in U.S. history.)
- By the end of 2001, the American Home Products Corporation paid more than $11.2 billion to settle about 50,000 consumer lawsuits related to the diet-drug combination of fenfluramine and phentermine, commonly known as "fen-phen." In addition, the company put aside $1 billion to cover future medical checkups for former fen-phen users and $2.35 billion to settle individual suits.
- Between 1971 and 1974, more than 5,000 product liability lawsuits were filed by women who had suffered severe gynecological damage from A. H. Robins Company's Dalkon Shield, an intrauterine contraceptive device. Although the company never recalled its product, it paid more than $314 million to settle 8,300 lawsuits. It also established a $1.75 billion trust to settle ongoing claims. The firm avoided its responsibility toward its customers by not considering a recall for nine years after the problem was known.

- Procter & Gamble's Rely tampon was pulled from the market in 1980 after 25 deaths were allegedly associated with toxic shock syndrome caused by tampon use.
- Firestone's problems first came to light in 1978, when the Center for Auto Safety said it had reports that Firestone's steel-belted radial TPC 500 tire was responsible for 15 deaths and 12 injuries. In October 1978, after attacking the publicity this product received, Firestone executives recalled 10 million of the 500-series tires. Firestone recently paid $7.5 million in addition to $350,000 to settle the first case in the Bridgestone/Firestone Ford Explorer crisis. Two hundred injury and death lawsuits have been settled since the recall, and it is estimated that it will cost $50 million to settle the lawsuits.
- A federal bankruptcy judge approved Dow Corning Corporation's $4.5 billion reorganization plan, with $3.2 billion to be used to settle claims from recipients of the company's silicone gel breast implants and the other $1.3 billion to be paid to its commercial creditors. A jury had already awarded $7.3 million to one woman whose implant burst, causing her illness. The company is alleged to have rushed the product to market in 1975 without completing proper safety tests and to have misled plastic surgeons about the potential for silicone to leak out of the surgically implanted devices. More than 600,000 implants were subsequently performed.

Johns Manville Corporation Asbestos Legacy: Still Paying, 2013

"They'll be following in our footsteps," said Robert A. Falise, chairman of the Manville Personal Injury Settlement Trust, which was created by the bankruptcy court to ensure a steady source of money to pay claims filed against Johns Manville Corporation (JM) by workers exposed to asbestos in their workplaces. The company will be responding to outstanding claims by asbestos victims and their families for several decades. In fact, "as of the first quarter of 2012, the trust had paid 773,990 claims in the amount of approximately $4.3 billion, and the trust expects to receive more claims."

In June 2000, the company was sold to Warren Buffett for $1.9 billion in cash and the assumption of $300 million in debt. The asbestos-related trust, created to pay claimants, received $1.5 billion. As of March 2001, the trust had paid more than $2.5 billion to 350,000 beneficiaries. There are still more than a half million claimants and another half million expected to file. Looking back, reviews of JM's social responsibility management of the complex web of issues surrounding its asbestos production are mixed.

Asbestosis, mesothelioma, and lung cancer—all life-threatening diseases—share a common cause: inhalation of microscopic particles of asbestos over an extended period of time. The link between these diseases and enough inhaled asbestos particles is a medical fact. JM is a multinational mining and forest product manufacturer, and it was a leading commercial producer of asbestos. As of March 1977, 271 asbestos-related damages suits were filed against the firm by workers. The victims claimed the company did not warn them of the life-threatening dangers of asbestos. Since 1968, the company has paid more than $2.5 billion in such claims. And since the 1950s, it has faced hundreds of lawsuits from workers: their estimated value is more than $1 billion. By 1982, JM was facing more than 500 new asbestos lawsuits filed each month. Consequently, in August 1982, the company filed for Chapter 11 bankruptcy in order to reorganize and remain solvent in the face of the lawsuits; the firm was losing more than half the cases that reached trial. The reorganization was approved, and a $2.5 billion trust fund was set up to pay asbestos claimants. Shareholders surrendered half their value in stock, and it was agreed that projected earnings over 25 years would be reduced to support the trust.

JM devised a settlement that gave the Manville Personal Injury Settlement Trust enough cash to continue meeting claims filed by asbestos victims. Under the settlement, the building products division stated it would give the trust 20% of Manville's stock and would pay a special $772 million dividend in exchange for the trust's releasing its right to receive 20% of Manville's profits. After the transaction, the trust would own 80% of Manville and have $1.2 billion in cash and marketable securities, plus $2.3 billion in assets. This transaction enabled JM to rectify its balance sheet. Also, it changed its name to Schuller Corporation.

After JM spent several years operating under Chapter 11 of the U.S. Bankruptcy Code, the company emerged with $850 million in cash, 50% of its common stock, a claim on 20% of the company's consolidated profits, and bonds with a face value of $1.3 billion. The trust is expected to pay 10% of an estimated $18 billion in present and future asbestos claims to 275,000 victims who already have filed claims.

JM's social responsibility toward its workers, the litigants, the communities it serves, and society has, at best, been uneven. Since 1972, the company has been active and cooperative with the U.S. Department of Labor and the American Federation of Labor and Congress of Industrial Organizations (AFL–CIO) in developing standards to protect asbestos workers. However, Dr. Kenneth Smith—the medical director of one of the firm's plants in Canada—refused in the 1970s to inform JM workers that they had asbestosis.

There is also the complication and confusion of evolving and changing legislation on asbestos. The U.S. Supreme Court, as stakeholder, has not

taken a stand on who is liable in these situations: Are insurance firms liable when workers are initially exposed to asbestos and later develop cancer, or are they liable 20 years later? Also, right-to-know laws are not definitive in state legislatures. Does that leave JM and other corporations liable for the government's legal indecision?

Of the original 16,500 personal injury plaintiffs, 2,000 have died since the reorganization in 1982. With Warren Buffet's purchase of the company and the asbestos trust solidified, the management of this issue for the company is over.

Note that companies continue to settle asbestos lawsuits. The Mesothelioma Reporter web site (www.mesotheliomareporter.org) tracks and reports these settlements. For example, a recent settlement was reported for Pfizer subsidiary Quigley Co. and others who were defendants in a trial "that alleged that they caused personal injury by exposure to asbestos. The asbestos sometimes caused mesothelioma." That web site reported *ABC News* as stating that "Pfizer will establish a trust for the payment of pending claims as well as any future claims. It will contribute $405 million to the trust over 40 years through a note, and about $100 million in insurance. Pfizer will also forgive a $30 million loan to Quigley." As with other corporate crises, the aftermath continues.

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QUESTIONS FOR DISCUSSION

1. Should asbestos victims' claims be the liability of Johns Manville or of the decision makers who authorized the work policies and orders?
2. Who was or is to blame for the asbestos-related deaths and injuries in this case?
3. Is the declaration of Chapter 11 bankruptcy and the creation of a trust the best or only solution in this case? Who wins and who loses with this type of settlement? Why?
4. What ethical principle(s) did Johns Manville's owners and officers use regarding this type of settlement? What principle(s) do you believe they should have used? Explain.

The *Exxon Valdez,* Second Worst Oil Spill in U.S. History: Twenty-Five Years Later, Exxon Still Hasn't Paid for Long-Term Environmental Damages

"A year after the *Exxon Valdez* ripped open its bottom on Bligh Reef [off the Alaskan coast] and dumped 11 million gallons of crude oil, the nation's worst oil spill is not over. Like major spills in the past, this unnatural disaster sparked a frenzy of reactions: congressional hearings, state and federal legislative proposals for new preventive measures, dozens of studies, and innumerable lawsuits." The grounding of the oil tanker on March 24, 1989, spread oil over more than 700 miles. Oil covered 1,300 miles of coastline and killed 250,000 birds, 2,800 sea otters, 300 seals, 250 bald eagles, and billions of salmon and herring eggs, according to the *Exxon Valdez* Oil Spill Trustee Council, which manages Exxon settlement money. Sounds somewhat like the BP oil disaster, doesn't it?

Fast forward to 2013, and note the following: "Today, government studies confirm that most of the populations and habitats injured by the spill have not fully recovered, and some are not recovering at all. Despite this, the government's Reopener claim focuses solely on remediating intertidal oil. Government studies report thousands of gallons of Exxon Valdez oil still in beaches today, that this oil is still 'nearly as toxic as it was the first few weeks after the spill,' that 'the remaining oil will take decades and possibly centuries to disappear entirely,' and that tests on nearshore animals 'indicate a continuing exposure to oil.'"

Exxon's failure to pay the $5 billion in assessed damages is noteworthy. "After 14 years of appeals, in 2008 the U.S. Supreme Court (invoking a peculiar 1818 maritime ruling) reduced the punitive judgment to only $507 million, with the appeals court adding another $470 million in interest.... Although Exxon has not paid the claim, the government spill account today has $195 million, much of which can be used to fund beach remediation work, in expectation that this will be reimbursed if and when Exxon finally pays the claim."

A grand jury indicted Exxon in February 1990. At that time, the firm faced fines totaling more than $600 million if convicted on the felony counts. More than 150 lawsuits and 30,000 damage claims were reportedly filed against Exxon, and most had not been settled by July 1991, when Exxon made a secret agreement with seven Seattle fish processors. Under that arrangement, Exxon agreed to pay $70 million to settle the processors' oil-spill claims against Exxon. However, in return for the relatively quick settlement of those claims, the processors agreed to return to Exxon most of any punitive damages they might be awarded in later Exxon spill-related cases.

Exxon paid about $300 million in damages claims in the first few years after the spill. However, "lawyers for people who had been harmed called that a mere down payment on losses that averaged more than $200,000 per fisherman from 1990 to 1994." Twenty-five years after the disaster, "the U.S. Justice Department and State of Alaska say they are still waiting for long overdue scientific studies before collecting a final $92 million claim to implement the recovery plan for unanticipated harm to fish, wildlife and habitat."

The charge that the captain of the *Exxon Valdez,* Joseph Hazelwood, had a blood-alcohol content above 0.04% was dropped, but he was convicted of negligently discharging oil and ordered to pay $50,000 as restitution to the state of Alaska and to serve 1,000 hours cleaning up the beaches over five years. Exxon executives and stockholders have been embroiled with courts, environmental groups, the media, and public groups over the crisis. Exxon has paid $300 million to date in nonpunitive damages to 10,000 commercial fishermen, business owners, and native Alaskan villages.

In 1996, a grand jury ordered Exxon to pay $5 billion in punitive damages to the victims of the 1989 oil spill. At the time that the fish processors had entered the secret agreement with Exxon, they did not know the Alaskan jury would slap the company with the $5 billion punitive damages award. One of the judges claimed that had the jury known about this secret agreement, it would have charged Exxon even more punitive damages. As of 2001, Exxon had not paid any of these damages. It is also estimated that with Exxon's reported rate of return on its investments, it makes $800 million every year on the $5 billion it does not pay. (The company would have made back the $5 billion it refused to pay with accrued interest by 2002.) Brian O'Neill, the Minneapolis lawyer who represents 60,000 plaintiffs in the suit against Exxon, stated, "I have had thousands of clients that have gone bankrupt, got divorced, died, or been down on their financial luck" while waiting for the settlement. Looking back on this case, the November 2001 federal appeals court ruling opened the way for a judge to reduce the $5 billion punitive verdict. (However, the 1994 jury award of $287 million to compensate commercial fishermen was not reduced.)

In 2004, the Environmental News Network (ENN) reported that local residents and several government scientists are still at odds as to "whether Exxon Mobil Corporation should be forced to pay an additional civil penalty for the spill.... The landmark $900 million civil settlement Exxon signed in 1991 to resolve federal and state environmental claims included a $100 million re-opener clause for damages that 'could not reasonably have been known' or anticipated."

EPILOGUE

On June 25, 2008, the Supreme Court reduced the previously determined $5 billion punitive damages award against ExxonMobil to $507.5 million. Since Justice Samuel A. Alito Jr. owns Exxon stock, he did not participate in the final decision. With regard to whether Exxon should be held accountable for Captain Hazelwood's irresponsibility in the case, the court split 4-to-4. "The effect of the split was to leave intact the ruling of the lower court, the United States Court of Appeals for the Ninth Circuit, which said Exxon might be held responsible."

Justice David Souter hinted in his last paragraph on behalf of the 5-to-3 majority that this decision reflected the rule he was announcing for federal maritime cases in the Exxon case, "a rule that generally dictates a maximum 1:1 ratio between a punitive damages award and a jury's compensatory award." In effect, by reducing the *Exxon Valdez* verdict to $500 million, the court set a 1:1 ratio by passing the $507.5 million compensatory damage portion of the jury's award in this case. Stakeholders were divided on the outcome of the case. It should be recalled that Exxon had previously paid over $2 billion during the past 19 years on environmental cleanup and $1.4 billion in fines and compensation to thousands of fishermen and cannery workers.

Exxon chairman and CEO Rex Tillerson recently stated that "We have worked hard over many years to address the impacts of the spill and to prevent such accidents from happening in our company again." A different reaction came from the hard-hit Alaskan town of Cordova, where fishermen and local businesses suffered bankruptcies and even suicides in the long aftermath of the crises: "The punitive damages claim 'was about punishing [Exxon] so they wouldn't do it somewhere else,' said Sylvia Lange, who owns a hotel and bar frequented by fishermen. 'We were the mouse that roared, but we got squished.'" As a result of the June 2008 Supreme Court decision, fishermen and others hurt by the disaster will receive about $15,000 instead of $75,000. Note that in 2007, ExxonMobil earned a record $40.6 billion in profits. The company could pay the punitive award with four days profits.

LaRue Tone Hosmer, a noted ethicist, stated, "The most basic lesson in accident prevention that can be drawn from the wreck of the *Exxon Valdez* is that management is much more than just looking at revenues, costs, and profits. Management requires the imagination to understand the full mixture of potential benefits and harms generated by the operations of the firm, the empathy to consider the full range of legitimate interests represented by the constituencies of the firm, and the courage to act when some of the harms are not certain and many of the constituencies are not powerful. The lack of imagination, empathy, and courage at the most senior levels of the company was the true cause of the wreck of the *Exxon Valdez*." Kiley Kroh, deputy

editor of the *Climate Progress* blog, stated that "Critics of the delay say the ongoing struggle to hold Exxon accountable for unanticipated environmental damages in Alaska offers clear lessons to be learned regarding the continuing process of determining BP's long-term liability for the *Deepwater Horizon* catastrophe, a spill that was 20 times larger than *Exxon Valdez*."

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QUESTIONS FOR DISCUSSION

1. Who was at fault in this case and why?
2. Should Captain Hazelwood have been convicted of criminal drunkenness in this case? If so, how would that have changed the outcome of the settlement? If not, why?
3. Did Captain Hazelwood settle his "debt" in this case by agreeing to serve 1,000 hours in cleanup time in Alaska? Explain.
4. Describe Exxon's ethics toward this disaster based on what it had paid over the years up to the June 15, 2008, Supreme Court decision.

5. How much should the 33,000 commercial fishermen, Alaska Native peoples, landowners, businesses, and local governments have been paid as compensation, and why?
6. Respond to Hosmer's statement. Do you believe this sentiment applies to all responsibilities of senior executives in corporations; that is, do they need to show imagination, empathy, and courage toward all their constituencies? Explain your answer.

Chapter Summary

Managing corporate social responsibility (CSR) from the corporate board of directors to the marketplace requires commitment, and significant time, effort, and resources from organizations. At stake is a company's reputation, and even survival. External regulation is also required to help define guidelines and practices for companies to act responsibly toward their stakeholders, communities, and society.

The corporation as social and economic stakeholder was presented from the perspectives of the social contract and covenantal ethic. Corporate social responsibility was also discussed from legal, ethical, philanthropic, and pragmatic viewpoints. Managing and balancing legal compliance with ethical motivation was illustrated by the Sarbanes-Oxley Act and the Revised Federal Sentencing Guidelines for Organizations. A section on legal and regulatory laws and compliance presented the complexity of areas in which corporations must navigate with federal, state, and local agencies before creating and distributing their products and services. A summary of recent corporate scandals was given to demonstrate the need for legal compliance in corporations. Arguments were offered to explain that legal compliance legislation and programs alone are necessary but not sufficient enough to motivate ethical and legal behavior in organizations.

Corporate responsibility toward consumers was presented by explaining these corporate duties: (1) the duty to inform consumers truthfully; (2) the duty not to misrepresent or withhold information; (3) the duty not to unreasonably force consumer choice or take undue advantage of consumers through fear or stress; and (4) the duty to take "due care" to prevent any foreseeable injuries. The use of a utilitarian ethic was discussed to show the problems in holding corporations accountable for product risks and injuries beyond their control.

The free-market theory of Adam Smith was summarized by way of explaining the market context governing the exchange of producers and buyers. Several limits of the free market were offered: that imperfect markets exist; the power between buyers and sellers is not symmetrical; and the line between telling the truth and lying about products is very thin. Economist

Paul Samuelson's "mixed economy" was introduced to offer a more balanced view of free-market theory and of the unrealistic demands often placed on corporations in marketing new products.

An overview of two classic business ethics cases, Johns Manville Corporation and the *Exxon Valdez* oil spill, were presented to illustrate how legal and regulatory agencies are part of a much broader stakeholder system involving communities and groups in the marketplace. Laws and regulations, as mentioned earlier, are necessary but not sufficient enough forces with which corporate leaders must adhere to in order to act fairly toward their constituencies while being profitable.

Questions

1. Identify a company or organization in the media or with which you are familiar that operates ethically. What are the reasons this company/organization is ethical? (You may refer to the leadership, management, products, or services of the organization.)
2. Do you believe that the Sarbanes-Oxley Act is *not* needed? Explain or offer a different argument.
3. Are the 2004 Revised Federal Sentencing Guidelines, in your opinion, helpful to organizational leaders and boards of directors in promoting more ethical behavior? Explain. What other actions, policies, or procedures would you recommend?
4. Which of the corporate crises summarized at the end of the chapter were you unfamiliar with? Do you believe these crises represent "business as usual" or serious breakdowns in a company's system? Why?
5. After reading the Johns Manville and *Exxon Valdez* summaries, identify some ways these crises could have been (1) avoided and (2) managed more responsibly after they occurred.
6. What was your score on the "Rank Your Organization's Reputation" quiz in Ethical Insight 4.3? After reading previous chapters in this book, how would you describe the "ethics" of your organization, university, or college toward its customers and stakeholders? Explain.
7. Do you believe the covenantal ethic and social contract views are realistic for large organizations like Bank of America, JPMorgan, ExxonMobil, and Citibank, or federal agencies like the FTC and the Department of Defense? Why or why not? Explain.
8. What is the free-market theory of corporate responsibility, and what are some of the problems associated with this view? Compare this view with the social contract and stakeholder perspectives of CSR.
9. If you had to select either the legal/compliance ("stick") approach or the voluntary/ethical compliance ("carrot") approach toward running a corporation, which would you choose, and why? What would be likely consequences (positive and negative) of your choice? Explain.

Exercises

1. In this chapter's opening case, why do you think it took such a large-scale security breach for TJX to start a serious corporate "ethics" program?
2. Outline some steps you would recommend for preventing future corporate scandals like Enron, WorldCom, and the subprime lending crisis based on the contents of this chapter.
3. If you were consulting with a large corporation's executive team and were asked to talk about how that team could think about a social contract including stakeholder management reasoning, what would you recommend? Write down your advice.
4. You have been invited as a student who has studied business ethics to present a case to a CEO, CFO, and ethics officer of a mid-size firm wanting to be Sarbanes-Oxley compliant. You have been asked to discuss and help them argue the pros and cons of implementing this law. Lay out your approach and arguments, and be ready to tell them what you would recommend they do and why.
5. A large company has invited you to join in a discussion with their legal and human resource officers about integrating ethics into and between their departments. They want your ideas. Use Figure 4.2 and any other ideas from this and previous chapters to outline what you would contribute. Write up a paragraph to share with your class/group.
6. Find a recent article discussing an innovative way in which a corporation is helping the environment. Explain why the method is innovative, and whether you believe the method will actually help the environment or simply help the company promote its image as a good citizen. Use parts of this chapter to evaluate your answer.

Real-Time Ethical Dilemma

My job requires that I lie every day I go to work. I work for a private investigation agency called XRT. Most of the work I do involves undercover operations, mobile surveillances, and groundwork searches to determine the whereabouts of manufacturers that produce counterfeit merchandise.

Each assignment I take requires some deception on my part. Recently I have become very conscious of the fact that I frequently have to lie to obtain concrete evidence for a client. I sometimes dig myself so deeply into a lie that I naturally take it to the next level, without ever accomplishing the core purpose of the investigation.

Working for an investigative agency engages me in assignments that vary on a day-to-day basis. I choose to work for XRT because it is not a routine 9-to-5 desk job. But to continue working for the agency means I will constantly be developing new untruthful stories. And the longer I decide to stay at XRT, the more involved the assignments will be. To leave would probably force me into a job photocopying and filing paperwork once I graduate from college.

Recently I was given an assignment which I believed would lead me to entrap a subject to obtain evidence for a client. The subject had filed for disability on workers' compensation after being hit by a truck. Because the subject refused to partake in any strenuous activity because of the accident, I was instructed to fake a flat tire and videotape the subject changing it for me. Although I did not feel comfortable engaging in this type of act, my supervisors assured me that it was ethical practice and not entrapment. Coworkers and other supervisors assured me that this was a standard "industry practice," and that we would go out of business if we didn't "fudge" the facts once in a while. I was told, "Do you think every business does its work and makes profits in a purely ethical way? Get real. I don't know what they're teaching you in college, but this is the real world." It was either do the assignment or find myself on the street—in an economy with no jobs.

Questions

1. What is the dilemma here, or isn't there one?
2. What would you have done in the writer's situation? Explain.
3. React to the comment, "Do you think every business does its work and makes profits in a purely ethical way? Get real. I don't know what they're teaching you in college, but this is the real world." Do you agree or disagree? Why?
4. Describe the ethics of this company.
5. Compare and contrast your personal ethics with the company ethics revealed here.

Cases

Case 9

Conscious Capitalism: What Is It? Why Do We Need It? Does It Work?

Introduction

Conscious Capitalism: Liberating the Heroic Spirit of Business (2013) is a best-selling book written by John Mackey, CEO of Whole Foods, and Rajendra Sisodia, a management professor at Babson College. A major tenet of the book states, "Conscious capitalism is an evolving paradigm for business that simultaneously creates multiple kinds of value and well-being for all stakeholders: financial, intellectual, physical, ecological, social, cultural, emotional, ethical and even spiritual. This new operating system for business is in far greater harmony with the ethos of our times and the essence of our evolving beings." The four core tenets underlying the business practices of conscious capitalism include "higher purpose and core values, stakeholder integration, conscious leadership and conscious culture and management." Mackey's Whole Foods business embodies these principles, as do several other selected companies that the book exemplifies. This case presents the purpose, goal, and need for conscious capitalism that, since the publication of the book, has now become a movement.

Why Conscious Capitalism?

Mackey and Sisodia's book is not the first to initiate a change in the ways businesses should change. In his review of *Conscious Capitalism,* Alan Murray states that "Capitalist guilt is nearly as old as capitalism itself, but it has seen a resurgence since the financial crises of 2007." Bill Gates called for a new system of "creative capitalism" in 2008 at a World Economic Forum in Davos, Switzerland. He was upset that pharmaceuticals paid more attention to baldness than curing global diseases like malaria. Michael Porter, a Harvard Business School professor, in 2011 called for "shared-value capitalism," arguing that business leaders were too occupied by short-term financial profits, more so than "the well-being of customers, the depletion of natural resources, the viability of suppliers, and the concerns of the communities in which they produce and sell." Mackey and Sisodia continue in this tradition, writing that "With few exceptions, entrepreneurs who start successful businesses don't do so to maximize profits. Of course they want to make money, but that is not what drives most of them. They are inspired to do something that they believe needs doing. The heroic story of free-enterprise capitalism is one of entrepreneurs using their dreams and passion as fuel to create extraordinary value for customers, team members, suppliers, society, and investors."

Since the fall of the Berlin Wall in 1989, it has been undisputed in business circles that capitalism and free markets are the best way to promote prosperity and grow economies internationally. Significant progress has been made since

the inception of free-enterprise capitalism. Many believe that most of the world's problems today, such as poverty, education inequality, and problems in undeveloped nations, can be solved through innovations brought about by free markets and free-enterprise capitalism. The poorest nations might be encouraged to embrace the ideas of free-enterprise capitalism to achieve similar successes as the developed countries, such as the United States, Japan, and others.

Free-enterprise capitalism is approximately 200 years old. Below is a partial list of accomplishments during the past two centuries, attributed to free-enterprise capitalism.

- Average income per capita on a global level has increased by over 1,000% since 1800.
- Average life expectancy globally has increased to 68 years, much greater than the historical average of 30 years.
- Two hundred years ago, 85% of the world's population lived on less than $1 a day in today's terms. Today that number is 16%.
- In just the last 40 years, undernourished people globally has decreased from 26% to 13%; if the current trend continues, it is estimated hunger will be virtually eliminated in the twenty-first century.
- Two hundred years ago, the world was almost completely illiterate and today 84% of adults have the ability to read.
- With economic freedom has come political freedom: 53% of people currently live in countries that have democratic governments elected by universal suffrage, compared to zero people 120 years ago.
- Two key factors that have led to the success of free-enterprise capitalism have been entrepreneurship and innovation, combined with freedom and dignity of those transacting business. Both are necessary for capitalism's continued progress going forward. Entrepreneurs are also to be admired in an economy devoted to free-enterprise capitalism because they are the drivers of innovation that improves our lives, companies' competitive position, and economies.

Why is Capitalism under Attack?

Despite the achievements of free-market capitalism, it is criticized by many around the world. Capitalism has a branding problem, in which its image has been tarnished for various reasons. Entrepreneurs driving capitalism should be admired, yet so many are vilified. Capitalism by many around the world is depicted as a zero-sum game, in which workers are exploited and consumers are cheated by business owners. Critics of capitalism argue that this alleged, intentional process results in greater inequality between the rich and the poor, fragmentation among communities, and environmental degradation, all with the motivation of making a profit. In this portrayal, business owners and entrepreneurs are depicted as being motivated by greed, seeking profit maximization as a way of doing business, since ethical theory claims that people will only pursue their self-interest at the expense of others.

Underlying reasons of capitalism's branding problem stem, in part, from the corporate scandals that rocked the United States in 2000–2002. Some of the more well-known scandals include Enron, WorldCom, Tyco, and Adelphia Cable, all of which involved executive mischief, causing widespread losses for investors, partners, and communities alike. The latest widespread scandal in the United States–the subprime lending crisis in 2008–led to the longest recession since the Great Depression. This crisis was caused by illegal and unethical actions of large corporations and companies across all levels of the financial sector. Many of the major banks were lending to those who did not qualify, and then securitizing those loans for sale to other banks and consumers. The rating agencies, who were getting paid fees by the major banks, evaluated all of these securitized mortgage products as AAA (risk-free). Consumers during that time were overwhelmed by debt that they could not afford. These actions resulted in a continuing widespread financial crisis that further divided Main Street from Wall Street and society in general from capitalism.

Mackey and Sisodia believe there are several reasons for the attacks on capitalism. First, they argue that there has been an intellectual hijacking of capitalism by economists and critics. These parties have placed capitalism in a narrow, self-serving identity helping to paint capitalism as a profit-maximizing machine. Second, many businesses are operating at a low level of consciousness regarding their purpose and the large impact they have on the world. Third, the industrial era that gave rise to a mechanistic view of business, in which employees were seen as resources of production, embraced the goal of receiving the most output from as little input as possible. And finally, expanding regulations and the size of the government has produced a mutant form of capitalism, dubbed "crony capitalism."

This biased thinking is prevalent in the consciousness of many today. Wall Street analysts must meet quarterly earnings projections for all public companies. Many of these analysts tend to view any stakeholder (other than stockholders) as net drainers of value; that is, if you pay employees more, you will earn less in profits. This is a misunderstanding among many today about business in general, which dates back to the turn of the twentieth century when so-called "robber barons" wielded vast sums of wealth and were not ashamed to flaunt it. For example, Cornelius Vanderbilt was alleged to have said the following when he was warned about violating the law: "Law? Who cares about the law? Hain't I got the power?"

This dated way of thinking, although seemingly still practiced by some as evidenced in the corporate scandals between 2000 and 2002, shows a low consciousness and moral concern for stakeholders, which can lead to unintended consequences that affect stockholders as well as stakeholders–and, in fact, the entire global economy. This zero-sum concept leads to short-term thinking and can inadvertently support reckless risk-taking among those driven only by short-term profits. If a company seeks only or mainly to maximize profits, it will pressure its entire supply chain to disregard real-time data and constraints. For example, suppliers who are continually dictated to provide product and services

to meet unrealistic goals may be rewarded for a few quarters, but in the long-term such suppliers will do one of three things: go out of business; do business elsewhere; or provide products of lower quality, all of which cause havoc to a company's supply chain. Other consequences, such as disregard for the environment and low employee engagement, have led to the public perception of corporations as greedy, selfish, exploitative, and untrustworthy. Mackey and Sisodia write that "Business is good because it creates value, it is ethical because it is based on voluntary exchange, it is noble because it lifts people out of poverty and creates prosperity." Capitalism is therefore challenged to become more "conscious" of its heroic nature.

In 2002, a Gallup poll delineated problems with the perceptions of corporations. The poll found that "90% of Americans felt that people running corporations could not be trusted to look after the interests of their employees, and only 18% thought that corporations looked after their shareholders. 43% believed senior executives were only in it for themselves." The *New York Times* was also quoted, stating "the majority of the public . . . believes that executives are bent on destroying the environment, cooking the books and lining their own pockets." One reason for distrust of executives, in addition to the 2000–2002 scandals, is exorbitant executive pay. The Institute of Policy Studies showed that the ratio of CEO to average employee salaries in 1980 was 42 to 1, in 1990 it was 107 to 1, and in 2000 it was 525 to 1. In recent years the ratio has declined to 325 to 1, however the discrepancy is still too large, even outrageous compared to all other professional pay-scale comparisons.

The public image spurred by recent corporate Enron and large banks' "too big to fail" crises caused by greed and reckless practices have tainted trust of businesses and even capitalism. Chris Meyer and Julia Kirby stated the following in a keynote address at Bentley University (Waltham, MA) on the future of capitalism: "We capitalists are stuck in two deep ruts right now. One of those ruts is an overemphasis on return on equity, as it has become one of the primary (if not *the* primary) barometer of success for a company." Meyer and Kirby argue that a fixture on return on equity alone is not an appropriate proxy of the value a company provides, and that by fixating on a single metric, business is committing social suicide. Meyer and Kirby also assert that businesses in general are obsessed with competition, which can be just as harmful as helpful. Competition in free markets has driven innovation in the past, as companies seek out competitive advantages with new products and ways to improve the world; but an infatuation with competition, simply for its own sake, will not help drive the innovation needed if people and companies are hindered from being collaborative and inspiring productive change. Former Dupont CEO Charles Holliday has stated that "Dupont's long history has shown us that no company, however strong and competitive, can go it alone. Involvement in outside organizations and endeavors is a way of learning and leading."

So, where do we go from here? The CEO of General Electric, Jack Immelt, is quoted in Rajendra Sisodia's book *Firms of Endearment* as saying, "To be a great company today, you have to be a good company." Under conscious capitalism,

good businesses make money by creating value for others, not only by maximizing profits. It is essential for free-enterprise capitalism to be grounded in an ethical system based on shared value creation for all stakeholders. To prosper, companies will have to shift mindsets and practices by listening to and learning from today's customers. This shift represents a change not only in what people want but also in how products should be designed both aesthetically and functionally. For businesses to reach full potential, a new paradigm must be created to move beyond the simplistic models toward a higher purpose and value creation for all parties. Conscious capitalism is one step in that direction.

What Is Conscious Capitalism?

Doug Rauch, former CEO of Trader Joe's and current CEO of Conscious Capitalism, Inc., defines conscious capitalism as "recognition that we are interconnected and interrelated. That business at its core is a story of us." Jack Canfield, one of my company's advisory board members, describes the conscious capitalism process as building "sustainable, trusting partnerships with people and the earth, adhering to the core values of respect, integrity, and ethics."

A distinction must be made, however, between conscious capitalism and corporate social responsibility (CSR)—some believe these are one in the same. CSR is generally defined as a company's efforts that go beyond what is required by regulators in terms of societal and environmental impacts. To further delineate the distinctions between conscious capitalism and CSR, Edward Freeman, a thought leader on stakeholder relationship management, has stated,

> Assume you are CEO and you are asked the following: Your company's products improve lives. Suppliers want to do business with your company because they benefit from this relationship. Employees really want to work for your company, and are satisfied with their remuneration and professional development. And you're a good citizen in the communities where you are located; among other things, you pay taxes on the profits you make. You compete hard but fairly. You also make an attractive return on capital for shareholder and other financiers. However, are you socially responsible? (Freeman, 2006, 4)

Freeman notes that CSR, although intended to be beneficial, actually helps to reinforce the "separation thesis" that business and society are two distinct entities. At its worst, the separation thesis can generate a destructive idea of capitalism, in which CSR becomes an add-on to business to help lessen the harsh consequences of doing capitalistic business. This style of thinking fails to recognize the central role business plays in the global improvement in the well-being and prosperity of mankind. CSR is generally seen as beneficial to and contributing positive impacts on societies. However, because of the separation thesis, people may still view capitalism as harmful and interpret CSR as an extension of business—not integral to corporations' actual functioning.

Freeman has therefore developed his own version of CSR (company stakeholder responsibility), which breaks down the separation thesis and describes business as an enterprise with moral ramifications, not needing the arm of social

responsibility. In this view, capitalism is a system of social cooperation working together to create value that could not be created by individuals. From Freeman's perspective, the idea of corporate social responsibility is unnecessary and the baseline for conscious capitalism (i.e., a stakeholder approach) is set.

The Four Tenets of Conscious Capitalism

The base of conscious capitalism lies in four tenets: higher purpose; stakeholder integration; conscious leadership; and conscious culture and management. To fully understand the tenets, further delineation is necessary. The tenet of higher purpose depicts the powerful and broad impacts business has on the world. These impacts can be much greater when business is based on a higher purpose that goes beyond just generating profits and shareholder value. Purpose is the reason a company exists. Yes, all companies need to make money to survive, but they do not survive to make money. Professions such as lawyers, doctors, teachers, etc., put an emphasis on public good and have purposes beyond self-interest; so should business. When entrepreneurs originally create their companies, the majority create them for a purpose, to fill a need in society. Having a higher purpose helps to create a high degree of engagement among all stakeholders, rallying around a singular idea. This helps catalyze creativity, innovation, and organizational commitment–all benefits of pursuing a higher purpose beyond profits.

The second tenet of conscious capitalism is stakeholder integration. This tenet is rather similar to the Freeman style of management discussed earlier. A stakeholder is considered to be an entity that impacts or is impacted by a business. Stakeholders include employees, suppliers, the environment, investors, and more. Conscious businesses recognize that stakeholders are interdependent and that their business must be organized to provide optimal value creation for all parties. Stakeholders cannot be treated as individuals because business is a world of interconnected parties. Optimizing value creation for all stakeholders enables the whole system to flourish, not just the company at the center. It also helps to create a harmony of interests among the interdependent stakeholders, so that each party knows it is part of a much larger ecosystem.

To achieve a commitment to the stakeholder approach, we revisit Freeman and his version of CSR, in which he states there are four levels of commitment. Level 1 is a basic value proposition, in which a company must ask itself how it makes its stakeholders better off and what the company stands for. Level 2 involves sustained cooperation among stakeholders, in which the principles and values are established to base everyday engagement between the parties. Level 3 deals with understanding broader societal issues. At this level, companies must ask themselves how the basic value proposition staged in Level 1 and the principles of Level 2 either fit or contradict key trends and opinions in society. Level 4 deals with ethical leadership, which falls under the third tenet of conscious capitalism.

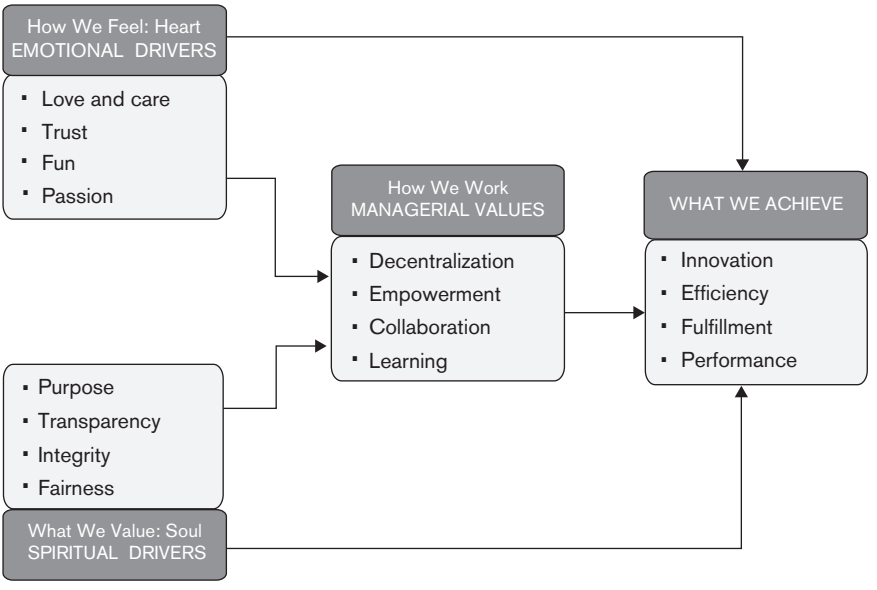
The third tenet of conscious capitalism is conscious leadership. Every conscious business needs a conscious leader; it is nearly (if not fully) impossible to

have a conscious business without a leader at the helm who shares the values of the firm and its higher purpose. To be a conscious leader, one must be motivated first and foremost by service to the higher purpose of the firm and creating value for all stakeholders. Conscious leaders reject the old model of fear-based command-and-control leadership and accept the "carrot and sticks" model as primary motivational tools. This model seeks to mentor, motivate, and inspire people into accomplishing their tasks and seeks to stimulate innovation and creativity over fear. Conscious leaders must also know what values and principles inform their leadership, their individual sense of purpose, and what they stand for as a leader. With conscious leadership in place, the fourth tenet of conscious capitalism becomes easier to achieve.

The fourth tenet of conscious capitalism is conscious culture and management. In a conscious business, the culture within the firm is a tremendous source of strength and continuity. This type of culture naturally evolves from the firm's and management's commitments to higher purpose, stakeholder interdependence, and conscious leadership. A pure focus on the first three tenets of conscious capitalism should ultimately lead to a conscious culture inspired by commitment, innovation, and creativity. Some may ask why culture is so important. A 2005 study by the Economist Intelligence Unit found that 56% of U.S. executives felt that the single greatest obstacle to growth for their firm was

Figure 1

Culture and Management Must Connect



Source: Based on a presentation that R. Sisodia gave at the 2012 Conscious Capitalism Conference at Bentley University, Waltham, MA.

corporate culture. Conscious businesses, because of their culture, do not face these obstacles on their path to growth. The key to establishing conscious culture and achieving the fourth tenet is to understand the connection between management and culture.

For conscious businesses to thrive, a conscious culture is necessary, which entails management promoting a different type of leadership style. The type of management approach to leadership can either magnify or depress the human need to care. Emphasizing a leadership style that connects what people feel and value to how people work promotes achievement beyond the ordinary scope of traditional businesses. The leadership style found in conscious businesses focuses on decentralization, empowerment, and collaboration. This style of management leads to an amplified ability of the firm to continuously innovate and create multiple kinds of value and wealth (not just financial) for all stakeholders as described by the flow chart in Figure 1, which illustrates the interconnectedness required between culture and management in conscious capitalism firms.

Firms of Endearment (FoEs)

So what exactly is a FoE? It is a "company that endears itself to stakeholders by bringing the interests of all stakeholder groups into strategic alignment. No stakeholder benefits at the expense of any other stakeholder group and each prospers as the others do." FoEs embrace a different idea than most companies. When looking at customers, they strive for share of heart, and not share of wallet. The theme with this form of thought is if you earn a share of the customer's heart, she will gladly offer you a bigger share of her wallet; do the same for an employee and that employee will give back with substantial increases in productivity and overall work quality. FoEs define the conscious capitalism movement and are at the forefront of conscious business practices, leading the business world into its much-needed evolution. FoEs include Amazon, Honda, Southwest, BMW, IDEO, Starbucks, CarMax, IKEA, Timberland, Caterpillar, JetBlue, Toyota, Commerce Bank, Johnson & Johnson, Trader Joe's, The Container Store, Jordan's Furniture, UPS, Costco, LL Bean, Wegmans, eBay, New Balance, Whole Foods, Google, Patagonia, Harley-Davidson, and REI.

FoEs have a distinct set of core values that help differentiate them from competitors. Some of the values have already been mentioned, such as aligning stakeholder interests. There is a laundry list of values distinct to FoEs, and it is pertinent to point out a few here. First, employee compensation and benefits are significantly greater than the standard for the company's category/industry, while executive salaries are modest, leading to a smaller ratio of CEO pay to average pay. FoEs also devote larger amounts of time to employee training than their competitors, part of the reason for lower FoE employee turnover than the industry average. FoEs consider corporate culture to be their greatest asset and therefore their primary source of competitive advantage. They seek to keep it that way by humanizing the company experience for customers and employees alike, by projecting a genuine passion and connecting emotionally.

From a FoE perspective, stakeholders are understood through the acronym SPICE, which stands for society, partners, investors, customers, and employees. Society is part of the local communities in which FoEs are embedded, as well as larger communities in need of resources for societal improvement. FoEs include governments and non-governmental organizations (NGOs) as well. Partners include upstream partners such as suppliers, as well as downstream partners such as retailers, thus representing the broad spectrum of what businesses would consider partners. Investors as a stakeholder include both individual and institutional shareholders, as well as lenders who have helped finance the company. Customers include both individual and organizational (business) customers, but extend beyond the current customer. FoEs view customers past, present, and future with equal affection and seek for share of heart from all. This is a similar viewpoint to how FoEs view employees. Employees past, present, and future are all stakeholders. Families are also included in their consideration of employees as stakeholders. All in all, FoEs have an extremely broad view of stakeholders and take each into equal consideration when planning firm strategy.

The best way to understand a FoE is to understand how one operates. For our purposes we will focus on Whole Foods as an example of a FoE. Mackey defines the values and concepts that have helped Whole Foods establish and maintain its conscious culture, as well as its competitive advantage against other grocers. For Mackey, purpose involves businesses needing to shift from profit maximization to purpose maximization in an effort to resurrect the brand of business. Purpose maximization is a powerful concept in that it drives everything the firm does. It aligns stakeholders by focusing on a purpose, and ironically, it typically results in making more money than ever thought possible (even more than profit maximization). Mackey further delineates Whole Foods' culture by discussing the concept of decentralization, which involves having 8–10 teams within each store and each team being self-managed. The teams are responsible for the operations of their specific store. They make decisions regarding hiring, product selection, merchandising, compensation, and more. Teams are rewarded through gain-sharing and not individual performance; 92% of Whole Foods stock options are granted to nonexecutives, whereas in a typical corporation, 75% of options will go to the top five executives. The key to this type of decentralization is that it empowers employees to make their own decisions. By allowing the teams to make decisions on their own, empowerment is greatly increased which helps lead to greater loyalty. Mackey claims that without empowerment, decentralization is useless.

Not only does Whole Foods focus on decentralization, but they also focus on authenticity and transparency, both of which foster trust. The current system of information-sharing in business is "need to know," which depresses trust within an organization. FoEs focus on being transparent with all stakeholders. Whole Foods accomplishes this by sharing all relevant financial information with team members, including compensation. Another FoE, The Container Store, is a private company and therefore has no obligation to share its financial information,

and yet the store shares all of its financial statements with all of its employees every year. Whole Foods also seeks to promote love and care within its organization. One way of doing so is through "Appreciations." Every meeting at Whole Foods is ended by one employee voluntarily expressing an appreciation for another employee, thus helping to shift the culture from judgment to love. All of this leads to continuous innovation, which is the key to having a sustainable competitive advantage. Lastly, Whole Foods is committed to collaboration, because innovation without collaboration is far less valuable. Collaboration combined with the other elements listed above is the recipe for success with Whole Foods and many FoEs, making them the truly great firms they are.

Conscious Capitalism: A Different View

The theme of this section has been touched upon throughout the case, but it is important for readers to remain focused on how conscious capitalism is an evolution and improvement of the current U.S. system of capitalism. Conscious capitalism opens up a different mindset. The trade-off thinking of the current system creates an "if/then" mindset leading to restricted options for managers. Conscious capitalism creates "both/and" thinking, which allows managers, entrepreneurs, and ambassadors of capitalism to open their mind to seemingly contradictory conditions, such as paying employees higher wages than industry averages and yet having higher profit margins than industry averages. Further, the "if/then" thinking leads to a zero-sum mindset, in which one stakeholder can only benefit at the expense of another and this system is becoming unsustainable for reasons illustrated previously. In order for value to be created by capitalism, each participant must make a profit; that is, each stakeholder must receive back more value than they originally invested. If stakeholders do not receive value from taking part in the system, they will eventually drop out. The exclusive pursuit of profit maximization has done enormous damage to this system and the reputation of capitalism as profit maximization, by definition, means giving as little and getting as much as possible. The conscious capitalism system of shared value creation increases opportunities by an order of magnitude as the mind breaks free of zero-sum, profit-maximization thinking.

The heroic story of free-enterprise capitalism is not one of profit maximization; it is one of entrepreneurs using their passion as fuel to create extraordinary value for customers, team members, suppliers, investors, and society. Business is far greater than just the sum of the individual stakeholders. Business is the interrelationship, interconnection, shared purpose, and shared values that various stakeholders of the business cocreate and coevolve together. FoEs and proponents of conscious capitalism do not view stakeholders as competing claimants on the value pool, but rather as active contributors to it. Overall, conscious capitalism creates a better environment than the current system. Companies motivated by higher purposes create sustained wealth for investors (see Figure 2); improve the lives of customers by satisfying their needs; elevate human satisfaction through fulfilling work; and build the social, cultural, infrastructural, and ecological wealth of society.

Conscious capitalism is, then, a revolution of traditional free-enterprise capitalism that opens up thinking to shared value creation for all stakeholders. Companies that follow this model are given the title "Firm of Endearment" and base their business models off trust, authenticity, innovation and more. These firms tend to pay employees more, work with suppliers to strengthen both firms, and have lower executive pay than most businesses today. The brand of business needs rejuvenation and conscious capitalism is at the forefront of revitalizing the natural good that business creates. But does conscious capitalism's business model provide financial success?

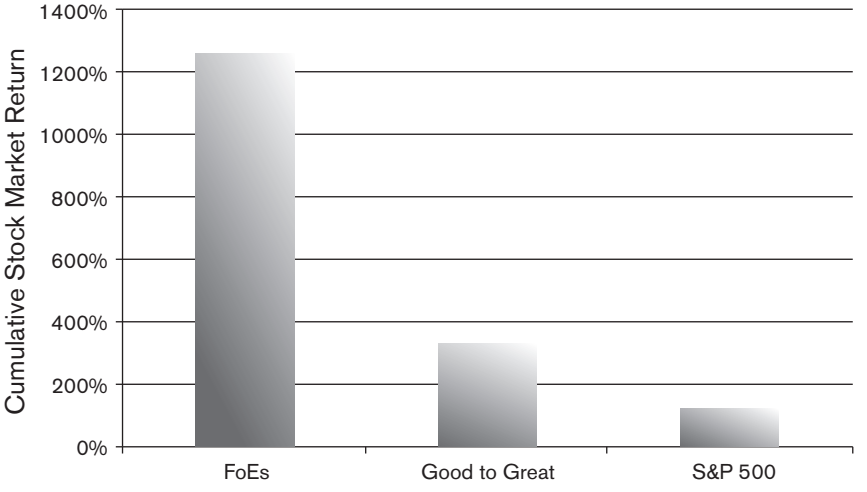
Conscious Companies

Presentation of Original Research

Critics of conscious capitalism argue that if employees are paid more, suppliers are treated well and paid a fair price, etc., these numbers should ultimately hit the bottom line of the conscious firms, thus affecting their stock price. Research has been done on this subject and provides amazing results. Studies on those firms that Mackey and Sisodia select and label as FoEs found that those companies generally earn higher shareholder returns, have premium price-to-earnings ratios, and earn a premium return on equity, all while incurring no more risk than the overall stock market. Over a 10-year time period, FoEs produced a cumulative return of 1,026%, while the S&P 500 managed only 122%. There was also another series of firms called "Good to Great," based on the James Collins book by the same title, with most of these firms focused strictly on profits. These firms

Figure 2

10-Year FoE Performance



Source: Sisodia, R., Wolfe, D., and Sheth, J. (2007). *Firms of endearment: How world-class companies profit from passion and purpose,* 137. Upper Saddle River, NJ: Wharton School Publishing.

also outperformed the S&P 500 but dramatically underperformed FoEs with a cumulative return of 331%, as seen in Figure 2. Note the comparison of FoEs' cumulative 10-year stock market performance (1,026%) with the exemplary company sample in *Good to Great* (331%), and to the S&P 500 (122%) for that same period.

Additionally, FoEs had an average price-to-earnings ratio of 26.8, while the S&P 500's was 18.4 and Good to Great companies' 16.8. Sisodia and his coauthors examined the average beta of these firms. Beta is the tendency of a security's returns to respond to swings in the market and is commonly used as a measure of risk. The average beta is that of the market (S&P 500), which is 1. A beta under 1 suggests that a stock, or group of stocks, is less risky than the overall market. Sisodia and his coauthors found that FoEs had an average beta of .92, thus leading to the conclusion that FoEs produce superior returns with less risk than the overall market, the ideal risk-return relationship for investors.

Updated Financial Analysis of FoEs

The research presented above was published in 2004 and included 17 public companies. An updated 2012 analysis consisted of 75 public companies split into four different tiers: highly conscious (elite); conscious; nearly conscious; and international. The "highly conscious" tier consists of 10 companies that embrace the four tenets of conscious capitalism. The "conscious" tier has 35 companies that embrace most aspects of conscious capitalism. These firms could improve one or two of the conscious capitalism tenets in order to be considered highly conscious companies. The "nearly conscious" tier consists of 12 firms that had one or two larger issues in their performance and record of conduct, indicating issues they had with at least one important stakeholder group. Finally, the "international" tier consists of 18 companies with headquarters and operations located outside the United States. Represented countries include India, Germany, the United Kingdom, and Canada.

Method of Analysis in Updated Study

The analysis used the four tiers noted above, comparing each tier individually to the S&P 500, Dow Jones Industrial Average (DJIA), and the Russell 3000. An analysis was also performed combining the firms in the "conscious" and "highly conscious" tiers, comparing them to the same three indices. The analysis dates back to 1997, with separate analyses done on the 3-, 5-, 10- and 15-year stock price performance of the selected firms. The study focused on the stock prices and beta of the selected firms, with the objective of duplicating the results found previously using a larger sample size and also showing the effects different levels of consciousness have on the financial performance of a company. Essentially, the hypothesis is that FoEs provide superior returns than the overall market with less risk.

The stock price and dividend data was pulled from Bloomberg terminals and was used to calculate quarterly holding period returns from 12/31/1997 to 12/31/2012. For firms that have been public less than 15 years, they were simply

added into the analysis once public stock price data became available. This was done so that not having a stock price (return would be zero) would not drag down the returns for overall index. The quarterly returns were then averaged together to create an index for each tier of firms. The quarterly returns for the index were then compounded to account for reinvesting dividends. The betas were also pulled from Bloomberg for the individual firms using a linear stock price regression from 12/31/1997 to 12/31/2012 and then averaged together to create an index beta for each tier of firms.

Results of the Analysis

The results of the financial analysis affirmed the previously published results regarding FoEs, even with the expansion to a larger number of firms including international firms. Figures 3 and 4 illustrate the cumulative and annualized performance of each tier of the firms explained above, in comparison to the S&P 500, DJIA, and Russell 3000. It is interesting to note that the "Elite FoEs" have the best performance of all the firms, with the "Conscious" (second tier) firms lagging the first tier but vastly outperforming the major stock indices. Finally, the "Nearly Conscious" firms still triple the performance of the major indices.

Another interesting observation is that the "Conscious International" firms also vastly outperform the market as a whole, validating that the model works

Figure 3

Results of Cumulative Performance of Tiered Firms

Cumulative Performance	**15 Years**	**10 Years**	**5 Years**	**3 Years**
Elite FoEs	2282.42%	498.81%	113.97%	98.40%
Conscious FoEs	1017.64%	305.03%	53.90%	47.94%
Combined FoEs	1271.90%	351.37%	67.69%	58.91%
Nearly Conscious	327.92%	195.30%	33.25%	45.41%
International FoEs	1109.64%	836.25%	39.20%	30.39%
S&P 500	98.11%	98.24%	8.55%	36.20%
DJIA	133.11%	102.31%	13.76%	36.14%
Russell 3000	106.96%	109.72%	10.61%	37.43%
Annualized Performance	**15 Years**	**10 Years**	**5 Years**	**3 Years**
Elite FoEs	23.54%	19.60%	16.43%	25.66%
Conscious FoEs	17.46%	15.01%	9.01%	13.95%
Combined FoEs	19.08%	16.27%	10.89%	16.69%
Nearly Conscious	10.18%	11.44%	5.91%	13.29%
International FoEs	18.08%	25.07%	6.84%	9.25%
S&P 500	4.66%	7.08%	1.65%	10.85%
DJIA	5.80%	7.30%	2.61%	10.83%
Russell 3000	4.97%	7.69%	2.04%	11.18%

internationally as well as domestically. It is also important to note the differences in returns over the different time periods. In the three-year analysis, while the selected firms still outperform the major indices, they do so by a smaller margin than the 5-, 10-, and 15-year analysis, with the gaps widening the longer the analysis is performed. This further supports the argument that the conscious business model is effective over the long-term performance of a company, both financially and socially.

The paradox of profits holds true as these firms do not pursue profit as their objective for being, as indicated previously, but rather pursue a higher purpose, enabling a more holistic view of what business can be. The argument that these firms cannot succeed financially is simply a fallacy as evidenced by the analysis presented here, as ultimately all financial performance is enveloped in the stock price of a firm.

In the updated beta analysis, there is a slight diversion from the research presented previously. The FoEs analyzed in *Firms of Endearment* had a beta of .92, while the firms in the updated analysis have betas slightly higher than 1, as shown in Figure 5.

Figure 4

Cumulative Performance Summary Comparing Fund Indices

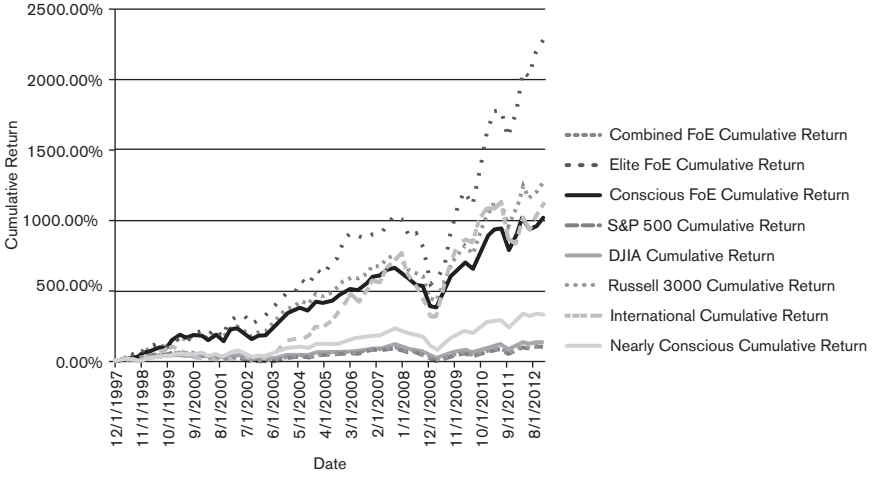


Figure 5

Beta of Indices

Elite FoEs	1.08
Conscious FoEs	1.05
Combined FoEs	1.07
Nearly Conscious	1.00

Source: John Warden's analysis.
Data from Bloomberg.

Although the betas of the firms are higher than the market average of 1, they are only slightly higher, and with their vast outperformance of the market it is fair to say that investors in these firms will tolerate slightly higher volatility. Also, the beta is only one measure of risk, measuring volatility. A long-term investor seeking firms that outperform the market over 3, 5, 10, etc., years is not as concerned with volatility as a Wall Street trader seeking to take advantage of day-to-day price movements. Essentially the point to be made is that these firms carry little to no extra risk in comparison to the overall market and yet vastly outperform the market over the long term.

Conclusion

Conscious capitalism's business model is timely, even long overdue. Businesses should not be solely focused on profits, but should adopt a more holistic approach to doing business. Conscious capitalism integrates all stakeholders, creating a greater pool of wealth for all involved in the ecosystem. Embracing conscious capitalism has proven to bode well for the companies that choose to do so. Conscious firms are healthy, growing businesses able to survive long-term, outperform competitors, and can generate outstanding returns in the stock market. Through the free markets and competition mechanisms of free-enterprise capitalism, it is my belief that firms embracing conscious capitalism will rise further to the top, and more companies will embrace the model as it becomes the only way to compete in the marketplace with shifting dynamics, wants, and needs. Conscious capitalism is the future of business.

Questions for Discussion

1. Why are the reasons conscious capitalism resurfaced an important topic in the press?
2. What are the basic principles and tenets of Mackey and Sisodia's book and the conscious capitalism movement that make it different from other related movements and similar topics?
3. What does ethics have to do with conscious capitalism as presented by Mackey and Sisodia?
4. Why is conscious capitalism not just a theory?
5. What do research results from the updated study in the article show?

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Case 10

Goldman Sachs: Hedging a Bet and Defrauding Investors

Securities Exchange Commission Charges Goldman Sachs

On April 16, 2010, the Securities and Exchange Commission (SEC) charged Goldman Sachs & Co. and one of its vice presidents with defrauding investors. During this time, the U.S. economy was in a state of severe recession following the subprime mortgage crisis. Goldman Sachs was charged with defrauding investors by misstating and omitting key facts about a financial product linked to subprime mortgages. The company had sold a financial product to investors created by the hedge fund Paulson & Co., which had bet against the success of the product. This case details the actions leading to the largest-ever settlement paid by a Wall Street firm to the SEC.

The ABACUS 2007-AC1 Product

Development of the ABACUS 2007-AC1 product began in 2007. It was a collateralized debt obligation (CDO). CDOs are based on the performance of subprime residential mortgage-backed securities. Paulson & Co., one of the largest and most profitable hedge funds, approached Goldman Sachs and paid the firm to structure a deal in which Paulson & Co. would add the mortgage securities to their portfolio. The hedge fund took a "short position" against the ABACUS product and the mortgage securities, betting on residential mortgages to fail. Placing the securities in a CDO would temporarily hide the true value of the loans and mislead investors; and when the loans went into default, the price of the product would plummet. Those who bet against the CDO stood to make significant profits.

On April 26, 2007, the transaction between Goldman Sachs and Paulson & Co. closed. Paulson & Co. paid Goldman Sachs $15 million to structure and market the ABACUS product. Paulson & Co. is one of the most profitable hedge funds in history, overseeing more than $32 billion in assets. Founded by John Paulson, a Harvard MBA graduate and one of the world's wealthiest people, the hedge fund had earnings in the tens of billions in each of the most recent fiscal years. The majority of Paulson's profits came from the collapse of the housing market. He predicted the billion-dollar write-downs of mortgage-backed securities and took advantage of that foresight. Paulson found subprime mortgages with adjustable rates in areas like California, Arizona, Florida, and Nevada—states that had experienced high increases in home prices that were severely inflated and would drop significantly.

Goldman Sachs knew of Paulson & Co.'s strategic approach to the ABACUS 2007-AC1. In marketing the ABACUS product, Goldman Sachs stated that the securities were selected by ACA Management LLC. ACA was a reputable third party with experience in residential mortgage-backed securities. Investors were not informed that Paulson & Co. had also played a significant role in selecting the

securities in the portfolio and that Paulson & Co. stood to benefit if the ABACUS securities defaulted. ACA and the other investors, IKB Bank, were still responsible for due diligence regarding the investment. While Paulson & Co. engaged in the selection process of the securities in the ABACUS portfolio, ACA analyzed and approved every security in the deal. ACA had the final authority over the securities included in ABACUS.

The fact that ACA, an objective third party, had the final approval in the selection of the portfolio was important to investors. IKB, a German bank, stated that if it had known of Paulson & Co.'s role in the selection of the mortgage-backed securities and their intended short position, it would not have invested in the product.

Goldman Sachs knew of the potential harmful consequences in selling the ABACUS product but chose to ignore the risks in favor of profits. CDOs were financial products that hedge funds like Paulson & Co. could bet on with very little risk. Goldman Sachs was not the only firm to engage in the practice of creating CDOs. More than $250 billion of these products were sold into the market in the two years leading up to the U.S. financial crisis. Many have speculated that a majority of these CDOs were deliberately designed to fail, similar to the ABACUS.

The Case against Fabrice Tourre

The man responsible for ABACUS was Fabrice Tourre. Tourre was a 31-year-old mid-level trader who'd been working at Goldman Sachs since 2001. Tourre foresaw the downfall of highly leveraged securities as early as 2005. He was one of the few who understood the complexity of the securities and saw an opportunity to help Goldman Sachs offset some of its impending losses. Tourre oversaw the ABACUS product from the beginning. He structured the transaction, marketed the product, and spoke directly with investors. With the knowledge that Paulson & Co. had designed ABACUS to fail, Tourre and Goldman Sachs chose not to disclose this information to investors. Tourre also misled the so-called third-party creators of ABACUS, ACA, into believing that Paulson & Co. had contributed approximately $200 million to the equity of ABACUS. Goldman Sachs again did not disclose that Paulson & Co.'s interests were contrary to ACA's.

Once the SEC lawsuit was filed, Goldman Sachs very quickly distanced itself from Tourre; continually declined to comment on Tourre's case; and even aided the SEC investigation of his actions. Tourre defended himself vigorously and claimed that he did not intentionally mislead investors. He stated that the marketing materials for ABACUS were incomplete and that additional information may have been needed. Many times, Tourre called himself "the Fabulous Fab." When asked if he regretted his actions, Tourre's only response was that he was "sad and humbled about what happened in the market." Tourre's actions received respect from Wall Street bankers and traders, who admired the way he foresaw the collapse in the housing market and, in turn, structured a lucrative deal for his client, Paulson & Co. In the banking industry, he was a legend.

The Downfall

ABACUS was created in April of 2007. It received a AAA rating from both credit-rating agencies, Moody's and Standard & Poor's. These agencies are never informed of the identity of the investors who participated in the deal. Due to the events surrounding the housing market bubble, the credit agencies' ability to rate securities was called into question.

During 2007, an internal conversation began within Moody's to determine whether lower ratings should be issued on CDOs and other deals involving mortgage bonds or other assets. It was determined that more evidence was needed to prove any deterioration in the housing market. Other rating firms acted similarly, choosing to ignore the signs of an impending collapse and allowing many ABACUS-like structured deals to enter the market.

By October 2007, 83% of the residential mortgage-backed securities in the ABACUS portfolio had been downgraded, and the remaining 17% were trending negative. By January 2008, 99% of the securities had been downgraded. The German Bank, IKB, investors into ABACUS 2007-AC1, allegedly lost more than $1 billion.

In April 2010, the SEC filed complaint charges against Goldman Sachs and Fabrice Tourre for the actions taken in structuring and marketing the ABACUS 2007-AC1. The SEC reported violations of section 17(a) of the Securities Act of 1933; section 10(b) of the Securities Exchange Act of 1934; and Exchange Act Rule 10b-5. The SEC was seeking injunctive relief, disgorgement of profits, prejudgment interest, and financial penalties. The chairman and CEO of Goldman Sachs, Lloyd Blankfein, spoke candidly and proclaimed that the day the suit by the SEC was filed was "one of the worst days in my professional life."

The Settlement

On July 15, 2010, Goldman Sachs entered into a settlement with the SEC, neither acknowledging any wrongdoing nor denying the SEC's allegations. In a statement made by Goldman Sachs, the only admittance made by the firm was "that the marketing materials for the ABACUS 2007-AC1 transaction contained incomplete information. In particular, it was a mistake for the Goldman marketing materials to state that the reference portfolio was 'selected by' ACA Management LLC without disclosing the role of Paulson & Co. Inc. in the portfolio selection process and that Paulson's economic interests were adverse to CDO investors. Goldman regrets that the marketing materials did not contain that disclosure."

The timing of the settlement announcement came only hours after the Senate had passed legislation to reform the U.S. financial system. Many saw this as political posturing by the SEC and a message for the rest of the financial industry. Goldman Sachs paid the SEC $550 million to settle the charges. It was the largest settlement ever paid to the SEC by a Wall Street firm. On the day the settlement was announced, Goldman Sachs' stock price rose over 4%. The settlement agreement ended three months of uncertainty with the firm. Investors saw it as a positive step, noting that top management was kept intact. The $550-million

figure was far lower than the anticipated $1-billion estimate predicted by many analysts.

In addition to the monetary settlement, Goldman Sachs was forced to make several internal changes. The firm was required to increase training for employees who deal with mortgage securities and increase oversight in the structuring and marketing of those securities. The settlement resulted in new industry-wide regulation. In its handling of Goldman Sachs, the SEC and its director of enforcement, Robert Khuzami, made it clear that the agency wanted to send a message not only to the firm, but to the entire industry.

Follow-up

Fabrice Tourre's battle, however, did not stop there. As the *New York Times* stated, "Mr. Tourre was found liable in August [2013] on six counts of civil securities fraud after a three-week jury trial in Lower Manhattan." He has since filed for a retrial (September 2013) because "there was a lack of evidence to support the jury's decision on some counts and that evidence was not presented to the jury in other instances." Tourre is still awaiting a judgment.

Reflections on Goldman Sachs and the ABACUS Product

The economic environment is often one of the primary forces behind stakeholder decisions, as in this case. The way in which the economic climate is trending may be a predictor of many business decisions. This was undoubtedly the case in Goldman Sachs' decision to structure, market, and sell CDOs. Goldman Sachs and Fabrice Tourre realized the impending collapse of the housing market and the resulting losses for the firm. Paulson & Co. also understood the economic climate and bet against the mortgage-backed securities that Goldman Sachs sold to investors.

The government and legal environment also made it possible for Goldman Sachs to engage in unethical practices. The lack of transparency in marketing materials for the ABACUS product was not uncommon. Investment banks were not forced to disclose to rating agencies the investors in the product, nor were they required to identify the security selection process. ACA, the objective third party, had the opportunity to review all the securities in the portfolio, as was their legal right, but because of the lack of a legal obligation for Goldman Sachs to disclose certain information, ACA was at a considerable disadvantage when it came time to evaluate many of the underlying assets in the portfolio.

Corporate Crisis Management Phases

An interesting aspect of the Goldman Sachs case was the reaction of the firm to the filing of the SEC lawsuit. The corporate social response stages in crisis management frameworks appropriately describe the experiences that characterized Goldman Sachs' dealing with the lawsuit. During the "reaction" stage—when the crisis first occurred—a firm is unsure of all the facts surrounding the crisis, but must look confident for its stakeholders. Goldman Sachs' stock plummeted when word of the lawsuit hit Wall Street. CEO Lloyd Blankfein categorically

denied any wrongdoing, insisting that the charges were fraudulent. This led to the second stage, "defense," when a firm's reputation is at risk and speculation arises as to the future of the firm. In Goldman's case, analysts were predicting billion-dollar fines and changes at the management level. The "insight" stage soon follows as a firm is forced to consider the fact that they may be at fault. To appease the SEC, Goldman Sachs not only conducted an internal review of the ABACUS product, but also of many similar products. This led to the fourth stage, "accommodation," when a firm acknowledges wrongdoing, apologizes, and reassures the public of its stability. Goldman Sachs apparently turned trader Fabrice Tourre into a scapegoat, distancing itself from him and claiming that he had control over the ABACUS product. The firm also settled with the SEC for a record sum, but still far short of the predicted estimates. The SEC vowed to implement regulation that would increase transparency in the marketing of complex securities, and Goldman Sachs pledged to increase oversight in the structuring and selling of these securities. Goldman Sachs' stock is higher at the time of writing than it was previous to the lawsuit.

Questions for Discussion

1. Was Goldman Sachs just taking advantage of a situational opportunity in the marketplace in this case? Explain and justify your answer.
2. Who, if anyone, was to blame for the illegal actions taken in this case and why or why not?
3. Who paid and at what "price" for the financial/economic and social costs of the transactions and results of transactions here?
4. Do the ends justify the means in this case, as it turns out? Explain and offer evidence.
5. What ethical and social responsibility lessons can you offer from this case and the aftermath? Explain.

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Case 11

Google Books

In October 2008, a broad class of authors and publishers, the Authors Guild, the Association of American Publishers, and Google announced a settlement agreement that will unlock access to millions of out-of-print books in the U.S. and give authors and publishers new ways to distribute and control access to their works online. If approved by the Court, the settlement will:

- Generate greater exposure for millions of in-copyright, out-of-print books, by enabling students, scholars, and readers to search, preview, and purchase online access to these works;
- Open new opportunities for authors and publishers to sell their copyrighted works and to maintain ongoing control over the ways those books can be displayed;
- Create an independent, not-for-profit Book Rights Registry that will locate and represent rightsholders, making it easier for everyone, including Google's competitors, to license works;
- Offer a means for U.S. colleges, universities, and other organizations to obtain subscriptions for online access to collections from some of the world's most renowned libraries;
- Provide free, full-text, online viewing of millions of out-of-print books at designated computers in U.S. public and university libraries; and
- Enable unprecedented access to the written literary record for people who are visually impaired.

The above settlement agreement continues to be controversial even after the revision. The Court denied the request for final settlement approval on March 22, 2011. The case then pinged back onto the desk of judge Denny Chin, who, to consider fair use, will have to look at issues such as the "purpose and character" of the copying.

Google has become synonymous with a new wave of companies seeking to become the leaders in their industries and make an impact on the world through creativity, social responsibility, and ethical behavior. Google began in 1996 as BackRub, a search engine project created by two Stanford Computer Science graduate students, Larry Page and Sergey Brin. Google has since built such strong brand recognition that it is now listed in the *Oxford English Dictionary* as a verb commonly used in everyday language. The company is known for its mission "to organize the world's information and make it universally accessible and useful." Google has created many tools and applications that have revolutionized how people use the Internet and access information. Google is now a leading search engine and major player in the advertising industry, with keyword advertising being the primary source of revenue and market capitalization.

Birth of Google Books

In 2003, Google began its development of Google Books, an online index of millions of books that can be previewed or read for free. The Google Print program,

which later became Google Book Search (Google Books) began in December 2003 as an "experimental program that indexes excerpts of popular books, blending the content from these works into regular Google search results." At this point in time, Amazon was already offering a service called "Search Inside the Book," which provided customers with screenshots of various pages of books, in some cases making the full text of a book available online. Initially, the Google Books project made only very brief excerpts available from search results. These short excerpts usually included only author biographies, jacket reviews, the inside jacket, or the book's introduction. Included along with the brief excerpts were links to purchase the book at Amazon, Barnes and Noble, and Books-A-Million. Booksellers did not have to pay for these links, nor did Google seem to benefit from any purchases resulting from these links. Google worked in partnership with various prominent publishing houses, such as Dell, Knopf, Random House, and Fodor's on this project and showed interest in "working with rights holders who own or control a 'substantial' amount of content for inclusion in the Google Print program."

In December 2004, the Google Print program partnered with the libraries of Harvard, Stanford, University of Michigan, Oxford, and the New York Public Library and began scanning books. In Google's announcement of this partnership, cofounder Larry Page explained that "Even before we started Google, we dreamed of making the incredible breadth of information that librarians so lovingly organize searchable online." This partnership and the digitizing of books was to be integrated with the Google index to make it searchable for users worldwide, "increas[ing] the visibility of in and out of print books . . . mak[ing] it possible to search across library collections including out of print books and titles that weren't previously available anywhere but on a library shelf . . . and generat[ing] book sales via 'Buy this Book' links and advertising."

Google Scholar

In May 2005, Google added "institutional access" to their Google Scholar program (the beta version was launched in October 2004), which allowed students and other researchers to "locate journal articles within their own libraries." Students and researchers were now provided an opportunity to "discover relevant information so they can build on the work of others and 'stand on the shoulders of giants.' "

Also in 2005, Google showed its support for writers and produced the first Mountain View book event with Malcolm Gladwell, author of *Blink* and *The Tipping Point.* This began the Authors@Google program, which has hosted more than 480 authors in 12 offices across the United States, Europe, and India.

Legal Implications

On September 20, 2005, the Author's Guild, Inc. and certain named individual authors brought a class-action suit against Google for copyright infringement by scanning library books and intending to use the scanned works on the Google web site without prior authorization from the authors/copyright owners. A month

later, a group of publishers brought a similar suit, alleging that Google had refused to obtain prior authorization from publishers for its Library Project, relying instead on the doctrine of "fair use." Google answered the publishers' complaint in 2005 and an amended class-action complaint in mid-2006, asserting affirmative defenses of the First Amendment of the United States Constitution (free speech) and "one or more of the exceptions to 17 U.S.C. § 106 [the exclusive copyright rights, including reproduction and public display, allegedly infringed] set forth at 17 U.S.C. §§ 107-122 [including "fair use," archival use and library use]." The "fair use" exception is set forth as follows:

> § 107. Limitations on exclusive rights: Fair use
> Notwithstanding the provisions of sections 106 and 106A, the fair use of a copyrighted work, including such use by reproduction in copies or phonorecords or by any other means specified by that section, for purposes such as criticism, comment, news reporting, teaching (including multiple copies for classroom use), scholarship, or research, is not an infringement of copyright. In determining whether the use made of a work in any particular case is a fair use the factors to be considered shall include–(1) the purpose and character of the use, including whether such use is of a commercial nature or is for nonprofit educational purposes; (2) the nature of the copyrighted work; (3) the amount and substantiality of the portion used in relation to the copyrighted work as a whole; and (4) the effect of the use upon the potential market for or value of the copyrighted work.

The fact that a work is unpublished shall not itself bar a finding of fair use if such finding is made upon consideration of all the above factors.

Because the entire book was scanned, factor (3) weighed against Google, who argued that only portions were made available for a particular search (see next section) and that its use was "transformative"–it didn't serve the same purpose as the copyrighted work relative to factor (1), and the effect of the search use actually promoted the market for the full copyrighted works, particularly out-of-print or obscure works under factor (4), nothwithstanding Google's commercial benefit through advertising under factor (1).

In August 2006, 100 libraries on 10 campuses of the University of California joined the Google Books Library Project and Google's Book Search began to offer free PDF downloads of books in the public domain. Google Books was able to offer its readers the ability to download and read PDF versions of out-of-copyright books. In the announcement of the new partnership, Google noted, "we do not enable downloading of any book currently under copyright. Unless we have the publisher's permission to show more, we display only small snippets of text–at most, two or three sentences surrounding your search term–to help you determine if you've found what you're looking for."

Google Patent Search

In December 2006, Google released Google Patent Search, which uses the same technology as Google Books Search. Utilizing the United States Patent

and Trademark Office (USPTO), Google Patent Search searches patents issued in the United States that are public-domain government information, and images of the entire database of U.S. patents readily available online via the USPTO web site.

The Legal Battle Continues

As a public debate over Google's fair use continued, the Google Books class action went through further proceedings. "In October 2008, Google announced a settlement agreement with a broad class of authors and publishers to make the world's books even more accessible online. If approved, the agreement will help readers access millions of hard-to-find, out-of-print books; it will provide new opportunities for authors and publishers to sell their works; and it will further the efforts of our library partners to preserve and maintain their collections while making books more accessible for people on their home computers, in their academic institutions, and in public libraries across the U.S."

The settlement provided a Registry overseeing copyrighted works for which payments would be made by Google for distribution to copyright holders and that works would be automatically included, unless the copyright holders expressly opted out. Since that time, hundreds of letters and formal objections have been filed with the court from authors and publishers who opted out. Many of these also objected to the control Google had over copyrighted works through the operation of the Registry. Although preliminarily approved, a fairness hearing for final approval of the settlement agreement was delayed.

In December 2008, Google expanded Google Book Search to include magazine articles by partnering with different publishers. This partnership gave access to the archives of magazines that were otherwise inaccessible to readers.

"On November 13, 2009, the parties to the settlement filed an amended agreement with the U.S. District Court for the Southern District of New York. Over the last several months, we have been carefully reviewing the submissions filed with the Court, including that of the Department of Justice. The changes made to the settlement were developed to address many of these concerns, while preserving the core benefits of the agreement."

The amended agreement created an "Unclaimed Works Fiduciary" to address the interests of those who had not yet claimed their works, and otherwise provided for negotiation of revenue splits. The court preliminarily approved the agreement on November 19, 2009, and a fairness hearing was scheduled for February 18, 2010. The U.S. Department of Justice filed an objection, stating in a press release that "the changes do not fully resolve the United States' concerns. The . . . amended settlement agreement still confers significant and possibly anticompetitive advantages on Google as a single entity, thereby enabling the company to be the only competitor in the digital marketplace with the rights to distribute and otherwise exploit a vast array of works in multiple formats."

The Appeal Court ruling is a very strong signal to Judge Denny Chin that fair use does indeed apply. "We believe that the resolution of Google's fair use defense in the first instance will necessarily inform and perhaps moot our analysis

of many class certification issues, including those regarding the commonality of plaintiffs' injuries, the typicality of their claims, and the predominance of common questions of law or fact," the ruling reads. As has been noted with regard to the "fair use" policy, "Google has been scanning all sorts of books and publishing them in the popular Google Books service. Books that are out of copyright are available in their entirety while books that are probably protected by copyright laws may be searched but only small snippets of the text are displayed to the user."

Judge Barrington D. Parker cited the "enormous societal benefit" that would result when someone at home in Muncie, Indiana, accessed books that otherwise would require a trip to a distant library. The judge also referred to the "logic of the thing" as he described how an academic author eager to get a treatise read by other researchers might welcome Google copying the work rather than collecting "a few dollars in damages because Google put it in their database."

The Authors Guild is seeking $750 in damages for each copyrighted book Google copied, which would cost Google more than $3 billion, Google attorney Seth Waxman said. The Authors Guild argues Google is not making "fair use" of copyrighted material by offering snippets of works. Google has defended its library, saying it is fully compliant with copyright law.

Google as a Stakeholder

Google's mission is altruistic by nature. The company handles its internal organization and employees by using an environment of trust in employees and their work ethic. Google achieves its well-known creative and casual workplace environment through an emphasis on "team achievements and pride in individual accomplishments that contribute to our overall success . . . put[ting] great stock in our employees–energetic, passionate people from diverse backgrounds with creative approaches to work, play and life." Fostering creativity in their employees has been a key attribute of Google and has truly set them apart from other companies. It has also brought about many innovative projects that Google and the greater world has been beneficiary to. Google makes a great priority of documenting these company ideals that align with their mission and references these ideals in all of their projects.

The way that Google has chosen to interpret and reinterpret its famous mission has been the center of much debate, not only in regard to Google Books but also its relationship with China. When Google first announced that it would be entering China, many of its historically largest supporters rallied to protest this expansion, citing that if the company entered China, it would be going against its mission because of the Chinese government's history of controlling what information citizens were allowed to access. Google chose to interpret its mission more broadly and argued that it was bringing information to a population that deserved search capabilities, notwithstanding some censorship. In recent months, Google has unfortunately struggled in China.

Among the stakeholders in this case are Google's employees, partners, clients/advertisers, and product developers. The public shareholders–who are

interested in higher share prices and possible dividends—may support Google Books and the settlement if it is likely to increase profits, without regard (necessarily) to Google's stated mission. Other stakeholders (with regard to the Google Books project) are the Authors Guild, their authors, publishers, libraries, schools and universities, their professors, current students, prospective students, alumni, newspapers, magazines, bloggers, independent writers, journalists and researchers, various advocacy groups, various law/research communities (which include the intellectual property community etc.), and Google's competitors, which include Amazon, Apple, and Microsoft. The other stakeholders that are in the broader reach are the U.S. government, various trade-industry groups, the print industry, international governments, and other far-reaching users.

Conclusion

Google programs like Google Books, Google Scholar, and Google Patent Search have the potential to serve as an invaluable resource by compiling and indexing research and works from countries across the globe. The compiling process, however, presents several ethical dilemmas—particularly regarding the ownership of works scanned and compiled. This has already been seen through lawsuits like the class-action suit brought by authors, publishers, the Authors Guild, and the Association of American Publishers, which resulted in the October 2008 settlement. The settlement has since fallen through and the class-action lawsuit was restarted by the Authors Guild in December 2011. The Authors Guild is demanding that Google pay authors for works scanned without permission. "Jim Pitkow, who sold a Web-search company to Google in 2001, said 'Google has probably spent hundreds of millions of dollars scanning books and that has not been legitimized.'" A new survey has shown, however, that authors are benefiting from their works being posted on Google Books and that the site makes works easier to find.

Google is working to address copyright and domain issues in order to make its index available to worldwide Internet searches and finally settle the long-standing battle with the Authors Guild.

Many issues are at stake for these various stakeholders and each of their perspectives could prove to have various impacts and meanings for Google. The most prominent viewpoint that has been at the heart of the debate is that of the authors, writers, and creators of the works that are being scanned and made available on Google Books. As statements on Google Books indicate, these stakeholders are made up of "supportive," "non-supportive," and "mixed blessing" stakeholders, as discussed in Chapter 2. Some authors, particularly lesser-known and poorly published ones, welcome the accessibility of their works to the public because of the Google indexing and search capabilities—these are like the lesser-known musicians unrepresented by record labels with their marketing power who welcomed file-sharing. Popular authors and publishers—like many popular musicians and the record labels—may find their work pirated in perfect and costless digital copies, directly diminishing the rewards for their efforts. Other stakeholders, including some authors, Google competitors along its

lengthy vertical chain, and the U.S. Department of Justice, are concerned about the power Google holds in controlling the Registry established in the settlement and amended settlement.

At the heart of authors' claims is copyright. In the United States, the Constitution, article I, section 8, clause 8, provides for the power of Congress "To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." Those who favor a limitation of authors' rights to restrict dissemination of their works often refer to this constitutional quid pro quo, arguing that copyright should support society's progress by limited incentives, which are secondary to the greater good. Of course, the same argument that supports Google's seeking a profit for providing digital means of dissemination of knowledge supports an author's seeking a profit for providing content to be disseminated.

Congress codified at 17 U.S.C. § 107, set out above, four factors to be assessed in determining a fair use exemption from copyright claims. This means that you can copy small parts for use in other works (such as a paper) as long as this was not for profit or would not affect the market for the copyrighted work. It also allows "transformative uses," such as the "Hairy Woman" parody of "Pretty Woman" by 2 Live Crew. Also, archiving (digitizing) of your own copies of books—for example, a library photocopying its decaying manuscripts—is specifically provided in law.

In the original Google Books project, university libraries were being archived, availing of the archive exception to copyright. As mentioned above, Google also defended the copyright infringement actions on the basis of the fair use of displaying snippets of a copyrighted work as results for keyword searches, arguing that this was a transformative use.

As mentioned, the early fear was the costless digital dissemination of copyrighted works, as exemplified by the digitization (MP3) and costless copying of music popularized first by Napster file-sharing. In an earlier, analog world, in the Betamax case, the Supreme Court found that damage to the market for copyrighted television programs by videotape recording for "time-shifting" was speculative, so such recording was fair use, which led to the development of the videotape industry. But videotapes could not be copied over and over again without degrading—unlike the perfect copies of digital music.

The debate, however, has now focused on the control of the distribution by Google. The question is control of pricing. In the one prominent digital music distribution scheme that has resulted in steady revenues, Apple's iTunes, Apple controls distribution by routinely updating its security code and by charging a single rate ($0.99) for a song, popular or unpopular. As expected, musicians (or more often, their recording labels) who are in greater demand complain that their songs should command higher prices (and royalties to them). Interestingly, Amazon followed a similar pricing strategy in its standard $9.99 for Kindle downloads, but is now challenged by Apple, who has attracted publishers by going to $19.99 for iPad downloads. Amazon has been forced to be more flexible in its

prices. Is freer flow of information promoted by lower, standard prices for books established by distributors such as Google, Amazon (contesting Google) and Apple (contesting Amazon)? Or do the in-demand content providers have the better argument that they should command higher prices?

The letter of the copyright law of fair use is not clearly determinative. Courts are moved by policy considerations and ethical concepts. Thus, the Betamax case turned in part because Fred Rogers testified at the trial court that he wanted children to be able to watch his program by time-shifting; that is, recording for later viewing.

Google did not go all the way to try its fair-use defense, but settled on a revenue splitting scheme that promises to help lesser-known authors to reap royalties. Whether the better-known authors and their publishers succeed in wresting control may depend on how well they assess the market at double the Amazon price.

In conclusion, Google's attempt to maintain its altruist mission, "to organize the world's information and make it universally accessible and useful," as supported by its need for revenues to support this effort, is aligned with some authors (lesser-known authors in need of exposure) and with its investors (on the revenue side), but it still conflicts with the claims to incentives by better-known authors and their publishers. In addition, Google's control of the Registry in the settlement is perceived by many (their competitors, the U.S., and international governments) as a threat to competition in the marketplace. While Google settled with some of the "non-supportive" stakeholders, they have yet to satisfy other authors who are still fearful that their work will be undervalued and pirated.

There is a moral tension between the "public good" rationale of the U.S. Constitution incentive to authors and a natural right that authors feel exists regardless of the aforementioned public good. In Europe, many have been rallying to fight the Google Books project, as they believe in authors' natural rights and "moral rights" to their creations. To maintain the integrity and control of one's creation is a principle shared by many and is itself thought of as the ultimate public good.

Questions for Discussion

1. In your opinion, should Google be allowed to copy books and post them online without the explicit knowledge and/or permission of the authors? Why or why not?
2. What control should authors have over the access to their works online?
3. If you were Google, would you have asked for permission prior to posting books or posted them and then asked for forgiveness when necessary? Explain. How does this reflect your personal ethics?
4. Do you think Google's strong brand recognition and size allows it to get away with more than other companies or individuals? Why or why not?
5. Is the Google Books idea fundamentally wrong? Why or why not? What potential benefits does it have to society?

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5

CORPORATE RESPONSIBILITIES, CONSUMER STAKEHOLDERS, AND THE ENVIRONMENT

5.1 Corporate Responsibility toward Consumer Stakeholders

5.2 Corporate Responsibility in Advertising

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5.3 Controversial Issues in Advertising: The Internet, Children, Tobacco, and Alcohol

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Notes

OPENING CASE

U.S. health care spending related to obesity in 2013 was $190 billion. The newly released United Nations (UN) report on global nutrition does not make for very uplifting reading: amid an already floundering global economy, the reality of a fattening planet is dragging down world productivity rates, while increasing health insurance costs to the tune of $3.5 trillion per year—or 5% of global gross domestic product (GDP).[1] Obesity in the workforce leads to expensive health care, interruptions in productivity, and days absent from work. Obesity and overall weight gain in the American population changed from a problem to a crisis when it was made an issue of public concern by the Food and Drug Administration (FDA) and the National Center for Health Statistics (NCHS). A survey conducted from 2007–2009 indicated that 34.4% of the U.S. adult population was overweight or obese.[2] An even more striking sta-

tistic is found in the weight increase experienced by children and adolescents in the United States. Current research estimates that 17% of children and adolescents (12.5 million children), ages 2 to 19, are overweight or obese. Higher prevalences of adult obesity were found in the Midwest (29.5%) and the South (29.4%). Lower prevalences were observed in the Northeast (25.3%) and the West (25.1%).[3] Carrying excess weight causes an increased risk for medical conditions, including coronary heart disease, stroke, hypertension, sleep apnea, and some forms of cancer. The rise in obesity comes despite efforts by First Lady Michelle Obama to promote healthy eating, and New York mayor Michael Bloomberg's size restriction on sugary drinks. The problem has become so profound that the U.S. Health and Human Services Department actually declared obesity a disease affecting the population in 2004. On June 18, 2013, the nation's largest physicians' group classified obesity as a medical "disease," despite the recommendations of a committee of experts who studied the issue for a year.[4]

In a 2006 survey of 1,000 households, conducted for *Medicine & Law Weekly,* results showed that 51% of the households would like to see fast food restaurants under the regulation of the government, while only 37% were opposed to such an action.[5] Consumers are suggesting that they are looking for more regulations to be placed on the fast food industry to provide them with a wider variety of healthier meal options.

Another reason cited for the overall increase in overweight and obese individuals in the United States is the ease of selecting calorie-packed foods and the high cost associated with eating healthy. The Centers for Disease Control and Prevention has pointed out that the availability of foods that are high in fat, sugar, and calories has made it increasingly more convenient for consumers to select those foods.[6] Availability is not the only factor at play. A downward trend in the cost of calories, combined with a downward trend in physical exertion at work, has also contributed significantly to the rise in obesity.[7]

Fast food chains have reacted to consumers' demand for healthier menus by making changes to their menus and marketing strategies. McDonald's has a new "Go Active" campaign, featuring new, healthy menu items, such as salads topped with chicken and a new fruit and walnut salad. Many of these changes have been targeted at children's nutrition. The "What's Hot in 2012" survey from the National Restaurant Association revealed the top-10 menu trends for 2012:

1. Locally sourced meats and seafood.
2. Locally grown produce.
3. Healthful kids' meals.
4. Hyper-local items.
5. Sustainability as a culinary theme.

6. Children's nutrition as a culinary theme.
7. Gluten-free/food allergy-conscious items.
8. Locally produced wine and beer.
9. Sustainable seafood.
10. Whole-grain items in kids' meals.

A report from the Yale University Rudd Center for Food Policy and Obesity noted that approximately 84% of parents with children aged 2 to 11 took their families to a fast food restaurant weekly. Although fast food restaurants are reevaluating their menus to include more healthful options for children, the study showed that of 3,039 kids' meal combinations possible, only 12 met the nutritional criteria for preschool-age children and only 15 met the criteria for older children.[8] Subway leveraged the story of Jared Fogle, the Indiana University student who once weighed 425 pounds. By making Subway's healthy sandwiches a part of his daily diet, and combining them with regular exercise, Fogle was able to lose 245 pounds in a year. On March 25, 2013, a leaked internal memo showed that McDonald's believed it would lose 22% of its 18–34-year-old customers to what's perceived as the healthier option, sandwich chain Subway, without adding the "wrap" onto its menu.[9]

The FDA has also joined the fight against obesity by initiating programs to "count calories." Its goals include pressuring fast food companies to provide more detailed and accurate information about nutrition content to their diners as well as educating consumers. With the partnership between the fast food chains and the FDA, consumers stand to be better informed about their options to become and remain healthy. Restaurants and company web sites now provide consumers with nutritional information for menu items. Restaurants have teamed up with nutritionists who can offer helpful suggestions. When presented with healthier options, it's in the hands of consumers to make the right choices to improve their health.

5.1 Corporate Responsibility toward Consumer Stakeholders

As the largest national economy in the world, the United States produced $16.2 trillion worth of goods and services (GDP) in 2012. China's growing economy earned it the second place slot, with a GDP of 8.2 trillion in 2012.[10] Consumer spending in the United States accounts for about two-thirds of total economic activity. Consumers may be the most important stakeholders of a business. If consumers do not buy, commercial businesses cease to exist. The late management guru Peter Drucker stated that the one true purpose of business is to create a customer.[11] Consumer confidence and spending are also important indicators of economic activity and business prosperity. Consumer

interests should be foremost when businesses are designing, delivering, and servicing products. Unfortunately, this often is not the case. As this chapter's opening case shows, giving customers what they want may not be what they need; also, not all products are planned, produced, and delivered with consumers' best health or safety interests in mind. Many companies have manufactured or distributed unreliable products, placing consumers at risk. The effects (and side effects) of some products have been life-threatening, and have even led to deaths, with classic cases being the alleged effects of the Merck drug Vioxx, the Bridgestone/Firestone tires on the Ford Explorer, tobacco products and cigarettes that contain nicotine, the Ford Pinto, lead-painted toys, and numerous other examples. At the same time, the majority of products distributed in the United States are safe, and people could not live the lifestyles they choose without products and services. What, then, is the responsibility of corporations toward consumer stakeholders?

Corporate Responsibilities and Consumer Rights

Two landmark books that inspired the consumer protection movement in the United States were Upton Sinclair's *The Jungle* (1906), which exposed the unsafe conditions at a meat-packing facility, and Ralph Nader's *Unsafe at Any Speed* (1965), which created a social expectation regarding safety in automobiles. Then *Fast Food Nation: The Dark Side of the All-American Meal* (2001) by Eric Schlosser, followed by *The Carnivore's Dilemma* (2008) by Tristram Stuart and Robert Kenner's 2008 documentary *Food, Inc.,* investigated the nature, source, production and distribution of food in the United States in particular. George Ritzer's *The McDonaldization of Society* (2011) drew attention to the pervasive influence of fast food restaurants on different sectors of American society, as well as on the rest of the world. In providing "bigger, better, faster" service and questionable food products, McDonald's has been the leader in creating—or reinforcing—a lifestyle change that, as the opening case shows, contributes to obesity. Morgan Spurlock's 2004 documentary, *Super Size Me,* also explored the fast food industry's corporate influence and encouragement of poor nutrition for profit.

As Steven Fink's issues evolution framework in Chapter 3 illustrated, a "felt need" arises from books, movies, events, and advocacy groups, and builds to "media coverage." This then evolves into interest group momentum, from which stakeholders develop policies and later legislation at the local, state, and federal levels. This same process has occurred and continues to occur with consumer rights. The books and documentaries mentioned here have contributed to articulating and mobilizing the issues of obesity, unsafe cars, and quality of life to the public.

The following universal policies were adopted in 1985 by the UN General Assembly to provide a framework for strengthening national consumer protection policies around the world. Consider which policies apply to you as a consumer:

1. *The right to safety:* to be protected against products, production processes, and services which are hazardous to health or life.
2. *The right to be informed:* To be given facts needed to make an informed choice, and to be protected against dishonest or misleading advertising and labeling.
3. *The right to choose:* to be able to select from a range of products and services, offered at competitive prices, with an assurance of satisfactory quality.
4. *The right to be heard:* to have consumer interests represented in the making and execution of government policy, and in the development of products and services.
5. *The right to satisfaction of basic needs:* to have access to basic essential goods and services, adequate food, clothing, shelter, health care, education and sanitation.
6. *The right to redress:* to receive a fair settlement of just claims, including compensation for misrepresentation, shoddy goods or unsatisfactory services.
7. *The right to consumer education:* to acquire knowledge and skills needed to make informed, confident choices about goods and services while being aware of basic consumer rights and responsibilities and how to act on them.
8. *The right to a healthy environment:* to live and work in an environment which is nonthreatening to the well-being of present and future generations.[12]

From an ethical perspective, corporations have certain responsibilities and duties toward their customers and consumers in society:

- *The duty to inform* consumers truthfully and fully of a product or service's content, purpose, and use.
- *The duty not to misrepresent or withhold information* about a product or service that would hinder consumers' free choice.
- *The duty not to force or take undue advantage* of consumer buying and product selection through fear or stress or by other means that constrain rational choice.
- *The duty to take "due care" to prevent any foreseeable injuries or mishaps* a product (in its design and production or in its use) may inflict on consumers.[13]

Although these responsibilities seem reasonable, there are several problems with the last responsibility, known as "due care" theory. First, there is no straightforward method for determining when "due care" has been given. What should a firm do to ensure the safety of its products? How far should it go? A utilitarian principle has been suggested, but problems arise when use of this method adds costs to products. Also, what health risks should be measured and how? How serious must an injury be? The second problem is that

"due care" theory assumes that a manufacturer can know its products' risks before injuries occur. Certainly, testing is done for most high-risk products; but for most products, use generally determines product defects. Who pays the costs for injuries resulting from product defects unknown beforehand by consumer and manufacturer? Should the manufacturer be the party that determines what is safe and unsafe for consumers? Or is this a form of paternalism? In a free market (or at least a mixed economy), who should determine what products will be used at what cost and risk?[14]

Related to the rights presented above, consumers also have in their implied social contract with corporations (discussed in Chapter 4) the following rights:

- *The right to safety:* to be protected from harmful commodities.
- *The right to free and rational choice:* to be able to select between alternative products.
- *The right to know:* to have easy access to truthful information that can help in product selection.
- *The right to be heard:* to have available a party who will acknowledge and act on reliable complaints about injustices regarding products and business transactions.
- *The right to be compensated:* to have a means to receive compensation for harm done to a person because of faulty products or for damage done in the business transaction.[15]

These rights are also constrained by free-market principles and conditions. For example, "products must be as represented: Producers must live up to the terms of the sales agreement; and advertising and other information about products must not be deceptive. Except for these restrictions, however, producers are free, according to free-market theory, to operate pretty much as they please."[16]

"Buyer Beware" and "Seller Take Care"

The age-old principle of "let the buyer beware" plays well according to free-market theory, because this doctrine underlies the topic of corporate responsibility in advertising, product safety, and liability. In the 1900s, the concept of "let the seller take care" placed responsibility of product safety on corporations[17] (which we discuss later in this chapter under product liability). Several scholars argue that Adam Smith's "invisible hand" view is not completely oriented toward stockholders.

Consumer Protection Agencies and Law

Because of imperfect markets and market failures, consumers are protected to some extent by federal and state laws in the United States. Five goals of government policymakers toward consumers are:

1. Providing consumers with reliable information about purchases.
2. Providing legislation to protect consumers against hazardous products.
3. Providing laws to encourage competitive pricing.
4. Providing laws to promote consumer choice.
5. Protecting consumers' privacy.[18]

Some of the most notable U.S. consumer protection agencies include:

1. *The Federal Trade Commission (FTC):* deals with online privacy, deceptive trade practices, and competitive pricing.
2. *The Food and Drug Administration (FDA):* regulates and enforces the safety of drugs, foods, and food additives, and sets standards for toxic chemical research.
3. *The National Highway Traffic Safety Administration (NHTSA):* deals with motor vehicle safety standards.
4. *The National Transportation Safety Board (NTSB):* handles airline safety.
5. *The Consumer Product Safety Commission (CPSC):* sets and enforces safety standards for consumer products.
6. *The Department of Justice (DOJ):* enforces consumer civil rights and fair competition.

Governmental and international agencies also work to protect consumers' legal rights. The Consumer World web site (http://www.consumerworld.org/pages/agencies.htm) has an extensive list of consumer protection agencies that includes the United States and international countries, including India, Hong Kong, Korea, Mexico, Canada, and Estonia, as well as other European countries. The strategic vision of the EU consumer policy "aims to maximise consumer participation and trust in the market. Built around four main objectives the European Consumer Agenda aims to increase confidence by: reinforcing consumer safety; enhancing knowledge; stepping up enforcement and securing redress; aligning consumer rights and policies to changes in society and in the economy."[19]

5.2 Corporate Responsibility in Advertising

Advertising is big business. Direct marketing advertising was 54.3% of the total advertising spending in 2009, while 2010 total direct marketing spending was estimated at $153.3 billion.[20] Figure 5.1 shows ad dollars spent by the industry in 4th quarter 2012 over 2011, according to Nielsen.

The extent to which advertising is effective is debatable, but because consumers are so frequently exposed to ads, it is an important topic of study in business ethics. The purpose of advertising is to inform customers about products and services and to persuade them to purchase them. Deceptive advertising is against the law. A corporation's ethical responsibility in advertising is to inform and persuade consumer stakeholders in ways that are not

Figure 5.1

Ad Dollars Spent by Selected Industry and Percentage Change Fourth Quarter 2012 over Fourth Quarter 2011

Industry	Ad Dollars Spent	Percent Change 4Q 2012 over 4Q 2011
Automotive	3,199,592,316	1%
Telephone service, wireless	1,239,133,625	28%
Restaurant, quick service	1,076,476,500	1%
Restaurants	451,942,094	6%
Pharmaceuticals	595,956,686	4%
Motion picture	821,495,375	–13%
Credit card service	454,255,844	–35%

Source: Adapted from Nielsen. (March 14, 2013). U.S. ad spend increased 2% in 2012 on strong Q3. *Nielsen.com.* http://www.nielsen.com/us/en/newswire/2013/u-s--ad-spend-increased-2--in-2012-on-strong-3q.html.

deceitful. This does not always happen, as the tobacco, diet, and fast food industries, for example, have shown.

Ethics and Advertising

At issue, legally and ethically for consumers, is whether advertising is deceptive and creates or contributes to creating harm to consumers. Although advertising is supposed to provide information to consumers, a major aim is to sell products and services. As part of a selling process, both buyer and seller are involved. As discussed earlier, "buyer beware" imparts some responsibility to the buyer for believing and being susceptible to ads. Ethical issues arise whenever corporations target ads in manipulative, untruthful, subliminal, and coercive ways to vulnerable buyers such as children and minorities. Also, inserting harmful chemicals into products without informing the buyer is deceptive advertising. The tobacco industry's use of nicotine and addictive ingredients in cigarettes was deceptive advertising.

The American Association of Advertising (AAA) has a code of ethics that helps organizations monitor their ads. The code cautions against false, distorted, misleading, and exaggerated claims and statements, as well as pictures that are offensive to the public and minority groups. The following questions can be used by both advertising corporations and consumers to gauge the ethics of ads:

1. Is the consumer being treated as a means to an end or as an end? And what and whose end?
2. Whose rights are being protected or violated intentionally and inadvertently? And at what and whose costs?

3. Are consumers being justly and fairly treated?
4. Are the public welfare and the common good taken into consideration for the effects as well as the intention of advertisements?
5. Has anyone been or will anyone be harmed from using this product or service?

The Federal Trade Commission and Advertising

The Federal Trade Commission (FTC) and the Department of Labor (DOL) are the federal agencies in the United States appointed and funded to monitor and eliminate false and misleading advertising when corporate self-regulation is not used or fails. Following is a sample of the FTC's guidelines:

> The FTC Act allows the FTC to act in the interest of all consumers to prevent deceptive and unfair practices. In interpreting Section 5 of the act, the Commission has determined that a representation, omission or practice is *deceptive* if it is likely to:
>
> • mislead consumers
> • affect consumers' behavior or decisions about the product or service
>
> In addition, an act or practice is *unfair* if the injury it causes, or is likely to cause, is:
>
> • substantial
> • not outweighed by other benefits
> • reasonably avoidable

The FTC Act prohibits unfair or deceptive advertising in any medium. A claim can be misleading if relevant information is left out or if the claim implies something that's not true. For example, a lease advertisement for an automobile that promotes "$0 Down" may be misleading if significant and undisclosed charges are due at lease signing. In addition, claims must be *substantiated,* especially when they concern health, safety, or performance. The type of evidence may depend on the product, the claims, and what experts believe is necessary. If your ad specifies a certain level of support for a claim (e.g., "tests show X"), you must have at least that level of support.

Sellers are responsible for claims they make about their products and services. Third parties—such as advertising agencies or web site designers and catalog marketers—also may be liable for making or disseminating deceptive representations if they participate in the preparation or distribution of the advertising or know about the deceptive claims.[21]

Pros and Cons of Advertising

Advertising is part of doing business, and not all advertising is deceptive or harmful to consumers. The arguments, both for and against advertising, raise awareness that provides information to both companies and consumers in

their production and consumption of information and transactions. General ethical arguments for and against advertising are summarized below.

Ethical Insight 5.1

Signs of an Advance-Fee Loan Scam: "Red Flags" from the FTC

- A lender who isn't interested in your credit history. A lender who doesn't care about your credit record should give you cause for concern. Ads that say "Bad credit? No problem" or "We don't care about your past. You deserve a loan" or "Get money fast," or even "No hassle—guaranteed" often indicate a scam.
- Fees that are not disclosed clearly or prominently. Any up-front fee that the lender wants to collect before granting the loan is a cue to walk away, especially if you're told it's for "insurance," "processing," or just "paperwork." Legitimate lenders often charge application, appraisal, or credit report fees. It's also a warning sign if a lender says they won't check your credit history, yet asks for your personal information, such as your Social Security number or bank account number.
- A loan that is offered by phone. It is illegal for companies doing business in the United States by phone to promise you a loan and ask you to pay for it before they deliver.
- A lender who uses a copy-cat or wannabe name. Crooks give their companies names that sound like well-known or respected organizations and create web sites that look slick.
- A lender who is not registered in your state. Lenders and loan brokers are required to register in the states where they do business. To check registration, call your state attorney general's office or your state's Department of Banking or Financial Regulation.

Source: Federal Trade Commission. (2012). Consumer Information, Advance-Fee Loans. http://www.consumer.ftc.gov/articles/0078-advance-fee-loans.

Arguments for Advertising

Arguments that justify advertising and the tactics of puffery and exaggeration include:

1. Advertising introduces people to, and influences them to buy, goods and services. Without advertising, consumers would be uninformed about products.

2. Advertising enables companies to be competitive with other firms in domestic and international markets. Firms across the globe use advertisements as competitive weapons.

3. Advertising helps a nation maintain a prosperous economy. Advertising increases consumption and spending, which in turn creates economic growth and jobs, which in turn benefits all. "A rising tide lifts all ships."

4. Advertising helps a nation's balance of trade and debt payments, especially in large industries, such as the food, automobile, alcoholic beverage, and technology industries, whose exports help the country's economy.

5. Customers' lives are enriched by the images and metaphors advertising creates. Customers pay for the illusions as well as the products advertisements promote.

6. Consumers are not ignorant. Buyers know the differences between lying, manipulation, and colorful hyperbole aimed at attracting attention. Consumers have freedom of choice. Ads try to influence desires already present in people's minds. Companies have a constitutional right to advertise in free and democratic societies.[22]

Arguments against (Questionable) Advertising

Critics of questionable advertising practices argue that advertising can be harmful for the following reasons. First, advertisements often cross that thin line that exists between puffery and deception. For example, unsophisticated buyers, especially youth, are targeted by companies. David Kessler, former commissioner of the FDA, referred to smoking as a pediatric disease, since 90% of lifelong smokers started when they were 18 and half began by the age of 14.[23]

Another argument is that advertisements tell half-truths, conceal facts, and intentionally deceive with profit, not consumer welfare, in mind. For example, the $300–$400 billion food industry is increasingly being watched by the FDA for printing misleading labels that use terms such as "cholesterol free," "lite," and "all natural." Consumers need understandable information quickly on how much fat (a significant factor in heart disease) is in food, on standard serving sizes, and on the exact nutritional contents of foods. This is increasingly relevant as food-marketing efforts increase. In 2010, for example, $1.24 trillion of food was supplied by food-service and food-retailing operations, which together make up the food-marketing system.[24] At stake in the short term for food companies is an outlay of between $100 million and $600 million for relabeling. In the long term, product sales could be at risk.

One of the great paradoxes of Americans today is their obsession with diet and health, while having one of the worst diets in the world. Also noted earlier, more than two-thirds of adults and more than one-third of children in the United States are obese or overweight. Food industry executives say that customers ask for low-fat food but rarely buy it. For many Americans, the problem is not just that they are consuming so much fat, it is that they don't know what they are eating. While government standards for weight and other recommended health-related metrics change, the 2010 government-recommended daily caloric intake of adult men in the United States is between 2,000 and 3,000, depending on age and the level of physical activity; the recommended calories for adult women is 1,600–2,400, also depending on age and level of physical activity. This range is still current in 2014. Many Americans far exceed those recommendations, in part because of their increasing reliance on restaurant food.[25]

Advertising and Free Speech

Because ads are often ambiguous, sometimes misleading, and can omit essential facts, the legal question of "free speech" enters more serious controversies. In commercial speech cases, there is no First Amendment protection if it can be proven that information was false or misleading. In other types of free speech cases, people who file suit must prove either negligence or actual malice.[26]

Should certain ads by corporations be banned or restricted by courts? For example, should children be protected from accessing pornography ads on the Internet? Should companies that intentionally mislead the public when selling their products be denied protection by the court?[27] The U.S. Supreme Court has differentiated commercial speech from pure speech in the context of the First Amendment. (See *Central Hudson Gas and Electric Corporation v. Public Service Commission*, 1980, and *Posadas de Puerto Rico Associates v. Tourism Company of Puerto Rico*, 54 LW 4960). Pure speech is more generalized, relating to political, scientific, and artistic expression in marketplace dealings. Commercial speech refers to language in ads and business dealings. The Supreme Court has balanced these concepts against the general principle that freedom of speech must be weighed against the public's general welfare. The four-step test developed by Justice Lewis F. Powell Jr. and used to determine whether commercial speech in advertisements can be banned or restricted follows:

1. Is the ad accurate, and does it promote a lawful product?
2. Is the government's interest in banning or restricting the commercial speech important, nontrivial, and substantial?
3. Does the proposed restriction of commercial speech assist the government in obtaining a public policy goal?
4. Is the proposed restriction of commercial speech limited only to achieving the government's purpose?[28]

For example, do you agree or disagree with the conservative plurality on the Supreme Court that has argued in the tobacco smoking controversy to give more free speech rights to tobacco companies? This has been suggested by Lawrence Gostin: "The [Supreme] [C]ourt has held that the FDA lacks jurisdiction to regulate cigarettes. The court observed that Congress, despite having many opportunities, has repeatedly refused to permit agency regulation of the product. Thus, Congress has systematically declined to regulate tobacco but has also preempted state regulation. Moreover, the Supreme Court's recent assertion of free speech rights for corporations prevents both Congress and the states from meaningfully regulating advertising. To the extent that commercial speech becomes assimilated into traditional political and social speech, it could become a potent engine for government deregulation. And, perhaps, that is the agenda of the court's conservative plurality."[29]

The commercial speech doctrine remains controversial. The Supreme Court has turned to the First Amendment to protect commercial speech (which is supposedly based on informational content). Public discourse is protected to ensure the participation and open debate needed to sustain democratic traditions and legitimacy. The Supreme Court has ultimate jurisdiction over decisions regarding the extent to which commercial speech, in particular, ads, and cases meet the previous four standards.

Recent judicial decisions regarding a number of areas, (including consumer privacy, spam, obesity, telemarketing, tobacco ads, casino gambling advertising, and dietary supplement labeling (see *Greater New Orleans Broadcasting Association Inc. v. United States* and *Pearson v. Shalala*) have sent the message that "The government's heretofore generally accepted power to regulate commercial speech in sensitive areas has been restricted." Regulators have prohibited certain advertisements and product claims based on the government's authority to protect public safety and the common good. The courts have sent the government (namely, the FDA) "back to the drawing board" to write disclaimers for claims it had argued to be inconclusive. The FDA's regulatory power has currently been curtailed.[30]

Paternalism, Manipulation, or Free Choice?

Moral responsibility between corporate advertisers and consumers can also be viewed along a continuum. At one end of a spectrum is *paternalistic control;* that is, "Big Brother" (the government, for example) regulates what consumers can and should hear and see. Too much protection can lead to arbitrary censorship and limit free choice. This is generally not desirable in a democratic market economy. At the other extreme of the continuum is *free choice* and *free speech* that are not regulated by any external government controls. Vulnerable groups—children, youth, the poor for example—may be more at risk from predatory advertisements, for example, unregulated pornography and scam advertising. Between these extremes, corporations develop ads to both create and meet consumer demand to buy products and services. The moral and commercial control corporations have in this space can constrain free choice through researched ads that range between puffery, ambiguity, exaggeration, half-truths, and deception to serve corporate interests. Ideally, corporations should seek to inform consumers fully and truthfully while using nonmanipulative, persuasive techniques to sell their products—assuming the products are safe and beneficial to consumer health and safety.

Enforcement of advertising can also be viewed along this continuum. Outright bans on ads can result in court decisions that determine a corporation's right to free speech under the Constitution. The latest such complaint comes from Columbia Law Professor (and former senior adviser to the Federal Trade Commission) Tim Wu in the *New Republic* article titled, "The Right to Evade Regulation: How Corporations Hijacked the First Amendment."

Wu criticizes court decisions protecting commercial speech rights as a return to the discredited Lochner era of the early twentieth century, when

some judges began interpreting the Due Process Clause as a license that allowed them to overturn economic legislation based on their own economic policy preferences.[31] At the other end of the spectrum, when actual harm and damage can be shown to have occurred as a result of and/or related to deceptive advertisements, the legal system intervenes. As moral and legal disputes occur over specific ads on the paternalism versus manipulation continuum, debate also continues as a matter of perception and judgment from different stakeholder views. In the following section, specific controversial issues of advertising online, children and youth as targets of advertising, and tobacco and alcohol ads are discussed.

5.3 Controversial Issues in Advertising: The Internet, Children, Tobacco, and Alcohol

Advertising and the Internet

Advertising on the Internet and cell phones presents new opportunities and problems for consumers. The ubiquity of Internet and cell phone communication and advertising is evident from these growing indicators:

- 4.85 billion people worldwide are expected to use mobile phones by 2015.
- 37% of consumers access social media on a mobile phone.
- 82 million Americans are expected to be using tablets by 2015.
- Mobile ad spending is expected to grow to $2.55 billion by 2014. This total includes spending for messaging, display, search, and video formats for mobile advertising.
- Total spending on mobile advertising will soar from roughly $8.5 billion this year to more than $31.1 billion in 2017, while overall online ad spending will grow from $42.3 billion to $61.4 billion during the same period. By 2017, eMarketer expects that about 60% of search ad spending will be devoted to mobile devices.
- Mobile is also forecast to account for a larger share of display dollars, though not quite to the same extent as search. By 2017, 48.4% of online display advertising (including banners, video, rich media, and ads such as Facebook's Sponsored Stories and Twitter's Promoted Tweets) will be on mobile devices (including tablets), up from an estimated 21.7% this year.[32]

In addition, YouTube's mobile business will generate approximately $800 million in 2013. According to Martin Pyykkonen, an analyst from Wedge Partners, YouTube accounted for about 10% of Google's $14 billion in sales in last quarter of 2013, with as much as 25% of YouTube revenues coming from mobile.[33]

The social networking web sites also draw large numbers of unique and returning viewers. For example, according to comScore, Inc.'s Video Metrix

service, Google Inc., including YouTube, drew 154 million unique viewers in March 2013 and Facebook Inc. had 64 million unique viewers in the same period. Over 182,000 million unique viewers in the United States watched 39.3 billion online videos during this same period. Video ad views totaled 13.2 billion.

Google sites topped the 2012 U.S. unique web visitors list with 191.4 million visitors; while Facebook drew overall viewer engagement with 10.8 percent of online minutes spent. Google, Facebook, Yahoo, Microsoft, AOL, and Amazon were the top six sites on both these metrics during the 2012 year.[34]

The ubiquity of ads on the Web continues to cause ethical problems, particularly for parents and those who wish to protect youth from a host of mobile media instant access via cell phones and pop-up ads, and exposure to web sites and advertisements dealing with sex, pornography, violence, drinking, and tobacco.

Pop-up and pop-under ads (ads that open up in a separate browser window) are used on some of the most visited web sites. In place of TV commercials that confront consumers with 30-second product introductions, the new "advertainment" shorts (also known as "commission content") that pop up on different mobile devices present product or service information to the viewer through a story. For example, Madonna starred in a BMW-funded film directed by her husband. "You're not using a product-based appeal, you're using an image-based appeal." It is important to mention that while stars such as Justin Bieber, Miley Cyrus, Lindsay Lohan, Lady Gaga, and Snooki draw attention to large numbers of virtual viewers in ads and infomercials, once their perceived and/or actual reputation is tainted, the attention can also turn.[35]

The Thin Line between Deceptive Advertising, Spyware, and Spam

In addition to undesirable pop-up ads and other aggravating forced online advertising, is the more serious problem of Internet spyware and spam—which problems are now global because of the Internet. The U.S. House of Representatives Judiciary Committee passed the Internet Spyware Prevention Act of 2004, predicting that the problem of spyware would be solved. The act carries penalties of up to five years in prison for using spyware that leads to identity theft. The Department of Justice was given $10 million to find ways to fight spyware and phishing—the act of sending email to a user falsely claiming to be an established legitimate enterprise. There have been other bills introduced by Congress to curb spyware and related Internet crimes.

The debate continues over whether or not congressional legislation and laws can stop Internet spyware and spam. Critics of congressional action alone argue that both industries and government must work to end spam and spyware.[36] Europe, also involved in solving cybercrime as well as daily scamming, takes a wider stakeholder involvement approach that includes legal

enforcement and educating industry representatives and consumers. The European Cybercrime Convention, sponsored by the Council of Europe, provides a treaty for combating global cybercrime. The cybercrime convention was approved by 30 countries, including Canada, Japan, South Africa, and the United States, and has been ratified by eight countries.[37] In December 2010, Canada's government passed the Canadian Anti-Spam Law (CASL), designed to regulate specific areas of electronic commerce, including what are known as commercial electronic messages (CEMs). These encompass SMS messaging, social media messaging, and e-mail communications. Although the enforcement date has not yet been set, enforcement is expected to begin in 2014.[38] Figure 5.2 shows the seriousness of Internet spam, spyware, and data breach statistics by industry.

The FTC has extensive guidelines for online advertising. For example, this governmental agency offers "Clear and Conspicuous Disclosures in Online Advertisements." The following is only a sample from the FTC web site.

When it comes to online ads, the basic principles of advertising law apply:

1. Advertising must be truthful and not misleading.
2. Advertisers must have evidence to back up their claims ("substantiation").
3. Advertisements cannot be unfair.[39]

Figure 5.2

Internet Spam, Spyware, and Crime

Data-Breach Statistics by Industry	
Industry	**Percent**
Medical / Health Care	38.9
Business	35.1
Educational	10.7
Government / Military	9.9
Banking / Credit / Financial	5.3
Annual Cyber-Crime Victim Estimates	
Victims per year	556 million
Victims per day	Over 1.5 million
Victims per second	18
Identities exposed	More than 232.4 million

Notes: Over 600,000 Facebook accounts occur each day. Fifteen percent of social network users reported that their profiles were hacked. Ten percent of social network users said they were victims of a scam or false link on social networks.

Source: Adapted from: Go-Gulf.com. (May 17, 2013). Cyber crime statistics and trends [Infographic]. *Go-Gulf.com.* http://www.go-gulf.com/blog/cyber-crime/.

The FTC's web site states that a particular disclosure is clear and conspicuous under the following conditions:

- the placement of the disclosure in an advertisement and its proximity to the claim it is qualifying;
- the prominence of the disclosure;
- whether items in other parts of the advertisement distract attention from the disclosure;
- whether the advertisement is so lengthy that the disclosure needs to be repeated;
- whether disclosures in audio messages are presented in an adequate volume and cadence and visual disclosures appear for a sufficient duration; and
- whether the language of the disclosure is understandable to the intended audience.[40]

The following section presents specific advertisement issues in the areas of children and youth (as targets) and tobacco and alcohol.

Advertising to Children

It is estimated that half of American children have a television in their bedroom, and "one study of third graders put the number at 70%. And a growing body of research shows strong associations between TV in the bedroom and numerous health and educational problems." With the advent of mobile phones, gaming consoles, tablets, laptops, smart TVs, and e-readers, children are exposed at early ages with access to the Internet. Microsoft asked 1,000 adults who were non-parents and parents, "How old is too young for kids to go online unsupervised?" Eight years old was the average age given that children were allowed independent Internet and device use.[41]

This is a disturbing number given the unlimited availability of and exposure to explicit sexual, pornographic, and other questionable content on ads and web sites, mixed with carefully crafted entertainment that is enhanced by new technologies. Should children and youth be exposed to the uncontrolled Internet through mobile phones and be able to log on from their computers, or from computers in libraries and cyber cafés, to web sites showing explicit sexual and pornographic pictures and videos? At issue is both how much protection can and should parents and guardians exert over children, and how much government protection through censorship does the public want? Although many telecom providers offer controls for parents, as do private firms through products such as CyberPatrol, CYBERsitter, and WebTrack, the issue also remains one of principle: How much regulation interferes with free speech for all? Moreover, file-sharing technologies and availability of pornography and other questionable content for children provide opportunities not only for users to see explicit material, but to share the content instantly.

Another ethical problem involves companies targeting children at too early an age—between 8 and 9 years old with ads. The phenomenon known as *age compression*—KGOY ("kids getting older younger")—refers to "tweens" (between childhood and teenage years). This market is targeted by such companies as Alberto-Culver, Estee Lauder, Procter & Gamble, and Unilever. The tween market was estimated to be between $7 and $8.5 billion in 2012. Marketing strategies include products such as youth hair care, cosmetics, and skincare.[42] Children at this age are more vulnerable to persuasive techniques.[43] Rosalind Wiseman, the author of *Queen Bees and Wannabes,* stated her opinion about the lack of responsibility of parents of children who are permitted to buy questionable products for their children's ages: "Mothers and fathers do really crazy things with the best of intentions. I don't care how it's couched, if you're permitting this [i.e., allowing the purchase of these products] with your daughter, you are hyper-sexualizing her. It's one thing to have them play around with makeup at home within the bubble of the family. But once it shifts to another context, you are taking away the play and creating a consumer, and frankly, you run the risk of having one more person who feels she's not good enough if she's not buying the stuff."[44]

Protecting Children

European, Asian, African, and North American countries are addressing issues on advertising to children. The Children's Online Privacy Protection Act (COPPA) and the FTC's implementing rule took effect April 21, 2000. Commercial web sites directed to children younger than 13 years old, or general audience sites that are collecting information from a child, must obtain parental permission before collecting such information. The FTC also launched a special site at http://www.ftc.gov/kidzprivacy to help children, parents, and the operators understand the provisions of COPPA and how the law will affect them.[45] In 1974, the Children's Advertising Review Unit (CARU) of the National Advertising Division of the Council of Better Business Bureaus was created to develop guidelines for self-regulating children's advertising (see http://www.caru.org/guidelines/guidelines.pdf). CARU approaches companies that violate COPPA. In May 2008, CARU recommended and received approval from the operator of the web site http://www.stardoll.com to "modify the site to assure it is in compliance with CARU's guidelines and the federal Children's Online Privacy Protection Act (COPPA)." CARU observed that the Stardoll web site offered "a virtual world where visitors can design fashions for paper dolls and play other dress-up games." When registering for basic membership on the site, visitors must first select one of the following two options: "12 year [*sic*] and under" or "13 year [*sic*] and under." Potential members who clicked on the "12 year and under" link were asked to enter their gender and a username, password, and e-mail address. Once that information was submitted, the next screen asked for a parent's e-mail address. After CARU requested changes to the web site, Stardoll decided to implement a neutral age-screening process and tracking mechanism.[46]

Advertising and media companies are also working with government agencies to change media strategies.[47] For example, the Media Monitoring Project (MMP) was created in South Africa because of increasing rates of obesity in children. The European Advertising Standards Alliance (EASA) and the European Sponsorship Association (ESA) joined together in January 2008 to form the Joint Arbitration Panel that will review "and adjudicate on consumer complaints about event sponsorship, an issue that is generally not covered in the ethical codes of most self-regulatory organisations (SROs) in Europe."[48]

Tobacco Advertising

Critics argue that tobacco and alcohol companies, in particular, continue to promote products that are dangerously unhealthy and that have effects that endanger others. According to the World Health Organization (WHO), cigarettes are "the only legal product that kills half of its regular users when consumed as intended by the manufacturer."[49]

Eighteen percent of American adults were cigarette smokers in 2012, according to a report released by the National Center for Health Statistics.[50] The tobacco industry spent approximately $8.2 billion in 1999 on traditional magazine direct-to-consumer advertising. Cigarette companies reportedly are targeting low-income women and minorities in their ads and focusing less on college-educated consumers. Three-thousand new teenagers and youth begin smoking each day. One out of three is predicted to die from tobacco-related illnesses—many when they are middle-aged.[51]

The Marlboro man, the infamous and now defunct Old Joe Camel, and other cigarette brands linked adventure, fun, social acceptance, being "cool," and risk-taking to smoking. Several new tobacco products have been produced to entice youth and smokers. "Cigarettes, smokeless tobacco, and cigars have been introduced in an array of candy, fruit, and alcohol flavors. R. J. Reynolds' Camel cigarettes, for example, have come in more than a dozen flavors, including lime, coconut and pineapple, toffee, and mint. Flavorings mask the harshness of the products and make them appealing to children; new smokeless tobacco products have been marketed as ways to help smokers sustain their addiction in the growing number of places where they cannot smoke. In addition to traditional chewing and spit tobacco, smokeless tobacco now comes in teabag-like pouches and even in dissolvable, candy-like tablets. . . . New products and marketing have been aimed at women, girls and other populations. The most recent example is R. J. Reynolds' Camel No. 9 cigarettes, a pink-hued version that one newspaper dubbed 'Barbie Camel' because of marketing that appealed to girls."[52]

Despite the fact that cigarette brand product placement in movies was banned by the 1998 Tobacco Master Settlement Agreement, cigarettes appeared in two out of three top-grossing movies in 2005. More than one-third of the movies were youth-rated films. The number of movies with tobacco-related scenes has gone down since 2005, but in 2010 more than 30% of top-grossing movies rated G, PG, and PG-13 had tobacco scenes.

And studies show that young people who see smoking in movies are more likely to start smoking.[53]

The Tobacco Controversy Continues

The tobacco controversy took yet another turn in 2004 when the DOJ brought the largest civil action against the tobacco industry, alleging that the industry defrauded and misled the public for 50 years regarding health risks of cigarette smoking. The DOJ requested $280 billion from the industry to repay its "ill-gotten" profits. A final judgment and opinion was issued in August 2006, finding big tobacco companies guilty of violating racketeering laws and defrauding the public. The U.S. Supreme Court made this ruling final in June 2010 by refusing to hear any further appeals. Tobacco companies are now prohibited from misleading and false advertising and must submit annual marketing data to the government. Ill-gotten profits must be surrendered to the government.[54]

William Schultz, a former DOJ lawyer who helped develop the case, states that, "What the government will argue is that the tobacco industry had a strategy to create doubt over health risks that made smokers more hesitant to quit, and those not smoking more likely to start. The fraud is that the companies knew about the health risks but created doubt and controversy about them to maintain their sales."[55] The lawsuit "has the potential to significantly transform the industry—forcing it to increase cigarette prices sharply, to change how it markets and promotes its product, and to spend billions for stop-smoking programs."[56]

The Supreme Court ruled unanimously in June 2001 that states have no right to restrict outdoor tobacco advertising near schools and public parks. The ruling, a victory for tobacco companies, followed a Massachusetts case that prohibited tobacco ads within 1,000 feet of public parks, playgrounds, and schools.[57] The 2001 ruling raised questions regarding the topic of advertising and free speech, for example: Does a corporation have the same free speech rights under the First Amendment to purchase advertising as people have to air political, social, and artistic views? For most of the nation's history, the Supreme Court has said that commercial speech (offering a product for sale) does not deserve the same protection as political speech. In a series of cases from the Rehnquist Court, "businesses were given powerful new First Amendment rights to advertise hazardous products."[58] While the battle between antismoking and prosmoking stakeholders continues, the paramount issue for antismoking proponents ranges from a total ban on all tobacco products to this statement by Dan Smith, president of the American Cancer Society Cancer Action Network: "The future is a smoke-free country where in public places, you can go and it's smoke free. I also think the future is much higher taxes on tobacco products."[59]

Alcohol Advertising

Alcohol abuse is the third-leading cause of preventable death in the United States.[60] The following statistics explain why:

- Percent of adults 18 years of age and over who were current regular drinkers (at least 12 drinks in the past year): 51.5%.
- Percent of adults 18 years of age and over who were current infrequent drinkers (1–11 drinks in the past year): 13.6%.
- Number of alcoholic liver disease deaths: 15,990.
- Number of alcohol-induced deaths, excluding accidents and homicides: 25,692.
- 79,000 annual deaths attributed to excessive alcohol use.

"Up to 40% of all hospital beds in the United States (except for those being used by maternity and intensive care patients) are being used to treat health conditions that are related to alcohol consumption," and approximately 15 million of the full-time employed workers in the United States are heavy drinkers of alcohol.[61] Almost 3 million children have serious alcohol problems but less than 20% get the needed treatment.

The Centers for Disease Control and Prevention report that "Alcohol is the most commonly used and abused drug among youth in the United States, more than tobacco and illicit drugs. Although drinking by persons under the age of 21 is illegal, people aged 12 to 20 years drink 11% of all alcohol consumed in the United States. Over 90% of this alcohol is consumed in the form of binge drinking. On average, underage drinkers consume more drinks per drinking occasion than adult drinkers. In 2008, there were approximately 190,000 emergency room visits by persons under age 21 for injuries and other conditions linked to alcohol."[62]

Alcohol ads also raise problems for consumers. Critics of alcohol ads argue that youths continue to be targeted as primary customers, enticed by suggestive messages linking drinking to popularity and success. Anheuser-Busch has been castigated for advertising its alcohol-heavy Spykes "Liquid Lunchables" which come in a colorful, two-ounce container in "kid-friendly flavors like Spicy Mango, Hot Melons, Spicy Lime, and Hot Chocolate." As the watchdog consumer nonprofit Center for Science in the Public Interest (CSPI) noted about this drink, "these so-called Spykes aren't juiceboxes, they're malt liquor with more than twice the alcohol concentration of beer."[63]

Ethical Insight 5.2

Are Minors (Individuals under the Legal Drinking Age) Personally Responsible for Their Voluntary Choices? Should Minors Be Punished as Adults?

On November 13, 2003, Ayman Hakki filed a lawsuit in Washington, DC, against several alcohol producers. The suit claimed that in an effort to create brand loyalty in the young, the defendants had deliberately targeted their television and magazine advertising campaigns at consumers under the legal drinking age for more than two decades.

Hakki asked for damages that included all of the profits the defendants had earned since 1982 from the sale of alcohol to minors. He also sought

class-action status for his suit. The plaintiff class consisted of all parents whose underage children had purchased alcohol in the last 21 years.

What is your opinion regarding the following quote? "Suits against tobacco and alcohol companies for targeting youthful purchasers reflect a particular philosophy regarding people under the legal drinking or smoking age: they are too immature to take full responsibility for their actions. This philosophy is in serious tension with the approach that has increasingly come to dominate our society's approach to juvenile criminal justice: when minors commit crimes, they ought to be held accountable and punished as adults."

Sources: Colb, S. F. (December 3, 2003). A lawsuit against "big alcohol" for advertising to underage drinkers. *FindLaw.com*. http://writ.news.findlaw.com/colb/20031203.html, accessed February 25, 2014. Social host liability. (author not identified). *FindLaw.com*. http://injury.findlaw.com/accident-injury-law/social-host-liability.html, accesssed February 25, 2014.

Product labeling and packaging are also two critical issues that are related to advertising. In a 2008 poll conducted by the Opinion Research Corporation, 1,003 Americans aged 21 and over were asked to identify the information that consumers consider most important on an alcohol label. The following results were reported:

- 77%: labels on products showing the alcohol content.
- 73%: the amount of alcohol shown in each serving.
- 65%: the calories shown in each serving.
- 57%: the carbohydrates in each serving.
- 52%: the amount of fat in each serving.

It was noted that "These findings reinforce a previous online survey conducted for *Shape Up America!* in December 2007, which reported that 79 percent of consumers would support alcohol labeling that summarizes the Dietary Guidelines' advice."[64]

5.4 Managing Product Safety and Liability Responsibly

Managing product safety should be priority number one for corporations. As a sign in one engineering facility reads, "Get it right the first time or everyone pays!" Product quality, safety, and liability are interrelated topics, especially when products fail in the marketplace. As new technologies are used in product development, risks increase for users.

How Safe Is Safe? The Ethics of Product Safety

Each year, thousands of people die and millions are injured from the effects of smoking cigarettes, and using diet drugs, silicone breast implants, and consumer products such as toys, lawn mowers, appliances, power tools, and

household chemicals, according to the Consumer Product Safety Commission (CPSC). But how safe is safe? Few, if any, products are 100% safe. Adding the manufacturing costs to the sales price to bolster safety features would, in many instances, discourage price-sensitive consumers. Just as companies use utilitarian principles when developing products for markets, consumers use this logic when shopping. Risks are calculated by both manufacturer and consumer. However, enough serious instances of questionable product quality and lack of manufacturing precautions taken occur to warrant more than a simple utilitarian ethic for preventing and determining product safety for the consuming public. This is especially the case for commercial products such as air-, sea-, and spacecrafts, over which consumers have little, if any, control.

Are cigarettes safe products? "Tobacco is the leading preventable cause of death in the United States. Cigarette smoking causes about one of every five deaths in the United States each year," about 443,000 deaths annually.[65]

Are other types of drugs safer than nicotine and additives in cigarettes? A metaanalysis (i.e., "the first comprehensive scientific review of both published studies and unpublished data that pharmaceutical companies have said they own and have the right to withhold") by the British medical journal, the *Lancet*, found that "most antidepressants are ineffective and may actually be unsafe for children and adolescents." This is an interesting finding in light of a recent Mayo Clinic study that found nearly 70% of Americans are on at least one prescription drug and more than half receive at least two prescriptions—many of which are antidepressants.[66]

The meta-analysis study reported that youth (ages 5–18) should avoid certain antidepressants—Paxil, Zoloft, Effexor, and Celexa—because of the risk of suicidal behavior with no benefit from taking the drug. Prozac was found an effective drug for depressed children and had no increased suicide risk.[67] Doctors signed more than 164 million prescriptions for antidepressants in 2008, according to IMS Health, making antidepressants one of the most prescribed drugs in the United States.[68] It is interesting to note that, according to the study, the British government recommended against the use of most antidepressants for children, except for Prozac. EU regulators have recommended against Paxil being given to children, and the U.S. FDA has requested drug manufacturers warn more strongly on their labels about possible links between the drugs taken by adolescents and "suicidal thoughts and behaviors."

Consumers also value safety and will pay for safe products up to the point where, in their own estimation, the product's *marginal value equals its marginal cost;* that is, people put a price on their lives whether they are rollerblading, sunning, skydiving, drinking, overeating, or driving to work.[69]

Product Safety Criteria: What Is the Value of a Human Life?

The National Commission on Product Safety (NCPS) notes that product risks should be reasonable. Unreasonable risks are those that could be prevented or that consumers would pay to prevent if they had the knowledge

and choice, according to the NCPS. Three steps that firms can use to assess product safety from an ethical perspective follow:[70]

1. How much safety is technically attainable, and how can it be specifically obtained for this product or service?
2. What is the acceptable risk level for society, the consumer, and the government regarding this product?
3. Does the product meet societal and consumer standards?

These steps, of course, do not apply equally to commercial aircraft and tennis shoes.

Estimates regarding the monetary value of human life vary. As Ethical Insight 5.3 illustrates, a recent methodology estimates the value of a human life at $129,000.

Ethical Insight 5.3

What Is the Value of a Human Life? $129,000

Stanford economists Stefanos Zenios and his colleagues at the Stanford Graduate School of Business used kidney dialysis as a benchmark. Every year, dialysis saves the lives of hundreds of thousands of Americans who would otherwise die of renal failure while waiting for an organ transplant. It is also the one procedure that Medicare has covered unconditionally since 1972, despite rapid and sometimes expensive innovations in its administration. To tally the cost-effectiveness of such innovations, Zenios and his colleagues ran a computer analysis of more than half a million patients who underwent dialysis, adding up costs and comparing that data to treatment outcomes. Considering both inflation and new technologies in dialysis, they arrived at $129,000 as a more appropriate threshold for deciding coverage. "That means that if Medicare paid an additional $129,000 to treat a group of patients, on average, group members would get one more quality-adjusted life year," Zenios says. Based on patient surveys, one "quality-of-life" year is defined as about two years of life on dialysis.

Take the $500,000 death benefit the government pays families when a soldier is killed in Iraq or Afghanistan. Or the cost calculations that for-profit health insurers make to determine how much coverage they'll give customers. In fact, at least some Americans seem at ease with allowing money to play a prominent role in health care decisions.

The study showed that for the sickest patients, the average cost of an additional quality-of-life year was much higher, at $488,000. "It is difficult to justify the burden and expense of dialysis when persons have other serious health conditions such as, for example, advanced dementia or cancer," says co-author Glenn Chertow, a nephrology professor at the Stanford School of Medicine. "In these settings, dialysis is unlikely to provide any meaningful benefit." But with organs, including kidneys, for transplant so scarce, is it

justifiable to deny these patients a chance to live through dialysis? It is a question, Zenios says, that everyone should approach with trepidation. "What is the true value of a human life? That's what we're asking people." He adds, "I wouldn't pretend to know."

Source: Kingsbury, K. The value of a human life: $129,000. (May 20, 2008). *Time.com*. http://www.time.com/time/health/article/0,8599,1808049,00.html, accessed January 8, 2014.

Regulating Product Safety

Because of the number of product-related casualties and injuries annually and because of the growth of the consumer movement in the 1960s and 1970s, Congress passed the 1972 Consumer Product Safety Act, which created the CPSC. This is the federal agency empowered to protect the public from unreasonable risks of injury and death related to consumer product use. The five members of the commission are appointed by the president. The commission has regional offices across the country. It develops uniform safety standards for consumer products; assists industries in developing safety standards; researches possible product hazards; educates consumers about comparative product safety standards; encourages competitive pricing; and works to recall, repair, and ban dangerous products. Each year the commission targets potentially hazardous products and publishes a list with consumer warnings. It recently targeted Cosco for the faulty product design of children's products. The death of an 11-month-old in July 1988 in a Cosco-designed crib was never reported by the company, even though the company began to redesign the product. Cosco was forced to pay a record $1.3 million in civil penalties to settle charges that it violated federal law by failing to report hundreds of injuries and the death.[71]

The CPSC is constrained in part by its enormous mission, limited resources, and critics who argue that the costs for maintaining the agency exceed the results and benefits it produces.

Consumer Affairs Departments and Product Recalls

Many companies actively and responsibly monitor their customers' satisfaction and safety concerns. A number of companies are using cell phone text messages to add more interactivity to their ads and consumer support. In addition, increased real-time mobile messaging, social networking services, Web browsing, and personal information management applications are being offered by some companies like Microsoft, to not only keep in touch with its customers but to also provide entertainment for them. Microsoft has teamed with Sony Ericsson Mobile Communications to give consumers more control over digital content.[72] Another way that companies can help consumers is by recalling their products when defects are noticed.

Many companies aggressively and voluntarily recall defective products and parts when they discover them or are informed about them. Mattel recalled over 700,000 toys in 2007 because of lead-paint issues. When unsafe products are not voluntarily recalled, the Environmental Protection Agency

(EPA), National Highway Traffic Safety Administration (NHTSA), FDA, and CPSC have the authority to enforce recalls of known or suspected unsafe products. Recalled products are usually repaired. If not, the product or parts can be replaced or even taken out of service. American autos are frequently recalled for replacement and adjustment of defective parts.

Amitai Etzioni, a noted business ethicist, argues that "There is, of course, no precise way of measuring how much more the public is willing to pay for a safer, healthier life via higher prices or taxes, or by indirect drag on economic growth and loss of jobs. In part this is because most Americans prefer to deal with these matters one at a time rather than get entangled with highly complex, emotion-laden general guidelines. In part it is also because the answer depends on changing economic conditions. Obviously, people are willing to buy more safety in prosperity than in recession."[73]

Product Liability Doctrines

Who should pay for the effects of unsafe products, and how much should they pay? Who determines who is liable? What are the punitive and compensatory limits of product liability? The payout in 2001 in litigation and settlements in diet-pill cases alone totaled $7 billion. Merck settled its Vioxx case with a $4.85 billion payout to settle approximately 50,000 lawsuits, with payouts beginning in August 2008. An additional $950 million was paid along with a guilty plea made to a criminal misdemeanor charge of illegally marketing Vioxx in November 2011. The $950 million includes a "$321.6 million criminal fine and $628.3 million to resolve civil claims that Merck sold Vioxx for unapproved uses and made false statements about its cardiovascular safety." In 2013 Merck agreed to pay $23 million to settle claims it duped consumers into buying the drug.[74]

Sixty companies have filed for bankruptcy court protection, and defendant companies and insurers have spent approximately $54 billion to date to settle asbestos liability-related lawsuits from products used in the 1970s. More than 600,000 asbestos-related suits have been filed, and many are still being resolved to this day. In February of 2012, for example, a $19.5 million settlement was offered as a part of the suit against W. R. Grace & Co. for the victims of asbestos exposure from its vermiculite plant located in Libby, Montana. A $43 million settlement was previously approved in 2011 for 1,128 victims of asbestos, approximately 400 of whom were killed.[75]

The doctrine of product liability has evolved in the court system since the early twentieth century, when the dominant principle of *privity* was used. Until the decision in *MacPherson v. Buick Motor Company* (1916), consumers injured by faulty products could sue and receive damages from a manufacturer if the manufacturer was judged to be negligent. Manufacturers were not held responsible if consumers purchased a hazardous product from a retailer or wholesaler.[76] In *MacPherson,* the defendant was ruled liable for harm done to Mr. MacPherson. A wheel on the car had cracked. Although MacPherson had bought the car from a retailer and although Buick had bought the wheel from

a different manufacturer, Buick was charged with negligence. Even though Buick did not intend to deceive the client, the court ruled the company responsible for the finished product (the car) because—the jury claimed—it should have tested its component parts.[77] The doctrine of *negligence* in the area of product liability was thus established. The negligence doctrine means that all parties, including the manufacturer, wholesaler, distributor, and sales professionals, can be held liable if reasonable care is not observed in producing and selling a product.

The doctrine of *strict liability* is an extension of the negligence standard. Strict liability holds that the manufacturer is liable for a person's injury or death if a product with a known or knowable defect goes to market. A consumer has to prove three things to win the suit: (1) an injury happened; (2) the injury resulted from a product defect; and (3) the defective product was delivered by the manufacturer being sued.[78]

Absolute liability is a further extension of the strict liability doctrine. Absolute liability was used in *Beshada v. Johns Manville Corporation* (1982). Employees sued Johns Manville for exposure to asbestos. The court ruled that the manufacturer was liable for not warning of product danger, even though the danger was scientifically unknown at the time of the production and sale of the product.[79] Medical and chemical companies, in particular, whose products could produce harmful but unknowable side effects years later, would be held liable under this doctrine.

Legal and Moral Limits of Product Liability

Product liability lawsuits have two broad purposes. First, they provide a level of compensation for injured parties, and second, they act to deter large corporations from negligently marketing dangerous products.[80] A California jury awarded Richard Boeken, a smoker who had lung cancer, a record $3 billion in a suit filed against Philip Morris in 2001. In 2007, a Los Angeles judge ruled for Boeken's 15-year-old son on an issue related to his lawsuit against Philip Morris, which he argued was liable for the death of his father. The $3 billion suit awarded earlier had been reduced to $55 million. Boeken (age 57) died in January 2002, seven months after the verdict. The disease had spread to his spine and brain.[81] The legal and moral limits of product liability suits evolve historically and are, to a large degree, determined by political as well as legal stakeholder negotiations and settlements. Consumer advocates and stakeholders (for example, the Consumer Federation of America, the National Conference of State Legislators, the Conference of State Supreme Court Justices, and activist groups) lobby for strong liability doctrines and laws to protect consumers against powerful firms that seek profits over consumer safety. In contrast, advocates of product liability law reform (for example, corporate stockholders, Washington lobbyists for businesses and manufacturers, and the President's Council on Competitiveness) argue that liability laws in the United States have become too costly, routine, and arbitrary. They claim liability laws can inhibit companies' competitiveness and willingness to innovate.

Also, insurance companies claim that all insurance-paying citizens are hurt by excessive liability laws that allow juries to award hundreds of millions of dollars in punitive damages because insurance rates rise as a result.

However, a two-year study of product liability cases concluded that punitive damages are rarely awarded, more rarely paid, and often reduced after the trial.[82] The study, partly funded by the Roscoe Pound Foundation in Washington, DC, is the most comprehensive effort to date to show the patterns of punitive damages awards in product liability cases over the past 25 years. The results of the study are as follows:

1. Only 355 punitive damages verdicts were handed down by state and federal court juries during this period. One-fourth of those awards involved a single product—asbestos.
2. In the majority of the 276 cases with complete posttrial information available, punitive damages awards were abandoned or reduced by the judge or the appeals court.
3. The median punitive damages award for all product liability cases paid since 1965 was $625,000—a little above the median compensatory damages award of $500,100. Punitive damages awards were significantly larger than compensatory damages awards in only 25% of the cases.
4. The factors that led to significant awards—those that lawyers most frequently cited when interviewed or surveyed—were failure to reduce risk of a known danger and failure to warn consumers of those risks.

A Cornell study reported similar findings.[83]

Furthermore, an earlier federal study of product liability suits in five states showed that plaintiffs won less than 50% of the cases; a Rand Corporation study that surveyed 26,000 households nationwide found that only 1 in 10 of an estimated 23 million people injured each year thinks about suing; and the National Center for State Courts surveyed 13 state court systems from 1984 to 1989 and found that the 1991 increase in civil caseloads was for real-property rights cases, not suits involving accidents and injuries.[84]

Contrary to some expectations, another study found that "judges are more than three times as likely as juries to award punitive damages in the cases they hear." Plaintiffs' lawyers apparently mistakenly believe that juries are a soft touch, and "they route their worst cases to juries. But in the end, plaintiffs do no better before juries than they would have before a judge." The study also found that the median punitive damages award made by judges ($75,000) was nearly three times the median award made by juries ($27,000).[85]

Product Safety and the Road Ahead

As outsourcing practices continue and new technologies are increasingly used in products, problems for both corporations and consumers will persist. Corporations face issues of cutting costs and increasing quality to remain competitive, while at the same time sacrificing some control over their manufacturing processes through outsourcing. Consumers must trust corporations'

ability to deliver safe and healthy products, including food, drugs, toys, automobiles, and medical products. Consumer stakeholders must rely on government agencies such as the FDA and the CPSC to monitor and discipline corporations that violate basic safety standards and practices. Consumers can also use the many watchdog nonprofit groups that monitor and advise on the quality of different projects. Consumer Reports (http://www.ConsumerReports.org) is one such organization. Corporations must rely on state-of-the-art monitoring and safety programs in their respective industries—such as Six Sigma (http://www.6-sigma.com), ISO 9000 (a quality assurance program), and other Total Quality Management (TQM) programs.

5.5 Corporate Responsibility and the Environment

There was a time when corporations used the environment as a free and unlimited resource. That time is ending, in terms of international public awareness and increasing legislative control. The magnitude of environmental abuse, not only by industries but also by human activities and nature's processes, has awakened an international awareness of the need to protect the environment. At risk is the most valuable stakeholder, the earth itself. The depletion and destruction of air, water, and land are at stake. Consider the destruction of the rain forests in Brazil; the thinning of the ozone layer; climatic warming changes from carbon dioxide (CO_2) accumulations; the smog in Mexico City, Los Angeles, and New York City; the pollution of the seas, lakes, rivers, and groundwater as a result of toxic dumping; and the destruction of Florida's Everglades National Park. At the human level, environmental pollution and damage cause heart and respiratory diseases and skin cancer. The top environmental concerns include climate change; energy, water, biodiversity, and land use; chemicals (toxics and heavy metals); air pollution; waste management; and ozone layer depletion.[86]

We will preview and summarize some of the issues to indicate the ethical implications. The purpose here is not to present in great detail either the scientific evidence or all the arguments for these problems. Rather, our aim is to highlight some issues and suggest the significance for key constituencies from a stakeholder and issues management approach and related ethical implications and concerns.

The Most Significant Environmental Problems

Toxic Air Pollution

More people are killed, it is estimated, by air pollution (automobile exhaust and smokestack emissions) than by traffic crashes. The so-called greenhouse gases are composed of the pollutants carbon monoxide, ozone, and ultrafine particles called particulates. These pollutants are produced by the combustion of coal, gasoline, and fossil fuels in cars. A 2013 American Lung Association report noted that "Still, over 131.8 million people—42 percent of the nation—live where pollution levels are too often dangerous to breathe," and

"roughly half the people (50.3%) in the United States live in counties that have unhealthful levels of either ozone or particle pollution." The top five most polluted cities 2013 by ozone levels are: Los Angeles, CA; Bakersfield, CA; Visalia, CA; Fresno, CA; and Sacramento, CA. The five most polluted cities at the time of writing by year-round particle pollution are: Bakersfield, CA; Visalia, CA; Phoenix, AZ; Los Angeles, CA; and Hanford, CA.[87] Figure 5.3 shows America's Top Five Global Warming Polluters.

Air pollution and greenhouse gases are linked to global warming, as evidenced in:

- The five-degree increase in Arctic air temperatures, as the earth becomes warmer today than at any time in the past 125,000 years.
- The snowmelt in northern Alaska, which comes 40 days earlier than it did 40 years ago.
- The sea-level rise, which, coupled with the increased frequency and intensity of storms, could inundate coastal areas, raising groundwater salinity.
- The atmospheric CO_2 levels, which are 31% higher than preindustrial levels 250 years ago.[88]

Nationally, carbon dioxide emissions are a major source of air pollution. America's top five warming polluters (by CO_2 emissions from company-owned or -operated power plants) are listed in Figure 5.3. These companies had estimated annual CO_2 emissions of 70 million tons and reported 2003 revenues of $4.4 billion.[89] Internationally, greenhouse gas emission statistics show that Spain had the largest increase in emissions, followed by Ireland, the United States, Japan, the Netherlands, Italy, and Denmark. The

Figure 5.3

America's Top Five Global Warming Polluters

Carbon Dioxide Emissions from Company-Owned or –Operated Power Plants	
Company	**Pollution**
American Electric	130,409,118 metric tons of carbon dioxide
Duke Energy Corporation	Released 1.89% of the nation's pollution
The Southern Company	Pumps out 1.76% of the nation's total greenhouse gases
Berkshire Hathaway	Controls interest in power plants, chemical factories, mining operations, and other industries that released more than 70 million equivalent metric tons of carbon dioxide in 2011
Ameren	Emitted 67,800,250 equivalent metric tons of carbon dioxide from their fossil fuel power plants.

Source: Adapted from Wall, T. (June 25, 2013). America's top 10 climate change polluters. *Discovery.* http://news.discovery.com/earth/global-warming/americas-top-10-air-polluters-130625.htm.

Figure 5.4

Global Non-CO_2 Percent Emissions Change in 6 Regions

Region	1990–2000	2000–2010	2010–2020	2020–2030	40-Year Total
OECD	1.2%	2.3%	14.6%	15.8%	37.3%
Non-OECD	12.1%	26.9%	17.2%	29.1%	115.2%
Europe and Eurasia (Non-OECD)	–30.2%	9.8%	11.1%	9.8%	–6.5%
Africa	0.6%	20.5%	10.5%	11.5%	49.2%
Central and South America	10.2%	19.8%	10.1%	9.2%	58.8%
Middle East	47.0%	24.9%	15.6%	18.4%	151.3%
Total	1.5%	16.3%	14.0%	18.5%	59.4%

Source: Adapted from Office of Atmospheric Programs Climate Change Division, U.S. Environmental Protection Agency. (2012). Summary report: Global anthropogenic non-CO2 greenhouse gas emissions: 1990–2030. http://www.epa.gov/climatechange/Downloads/EPAactivities/Summary_Global_NonCO2_Projections_Dec2012.pdf.

EU, Britain, and Germany had emission decreases during this period (see Figure 5.4).

To stabilize the climate, global carbon emissions must be cut in half, from the current 6 billion tons a year to under 3 billion tons a year. This reduction can be accomplished by producing more efficient cars and power plants, using mass transit and alternative energy, and improving building and appliance standards. These changes would also help alleviate energy crises as well as global warming and air pollution.[90]

Water Pollution and the Threat of Scarcity

Approximately 1 billion people worldwide lack access to improved water sources. This lack of access comes with a heavy price. Some 2 million deaths a year worldwide are attributable to unsafe water and to poor sanitation and hygiene, mainly through infectious diarrhea. Cholera is still reported to the World Health Organization (WHO) by more than 50 countries, and about 260 million people are infected with schistosomiasis. Unsafe levels of arsenic and fluoride in water supplies have exposed millions to cancer and tooth damage. The "increasing use of wastewater in agriculture is important for livelihood opportunities, but also associated with serious public health risks. 4% of the global disease burden could be prevented by improving water supply, sanitation, and hygiene."[91]

Water pollution is a result of industrial waste dumping, sewage drainage, and runoff of agricultural chemicals. The combined effects of global water pollution are causing a noticeable scarcity. Water reserves in major aquifers are decreasing by an estimated 200 trillion cubic meters each year. The prob-

lem stems from the depletion and pollution of the world's groundwater. "In Bangladesh, for instance, perhaps half the country's population is drinking groundwater containing unsafe levels of arsenic. By inadvertently poisoning groundwater, we may turn what is essentially a renewable resource into one that cannot be recharged or purified within human scales, rendering it unusable."[92] It is estimated that the United States will have to spend $1 trillion over the next 30 years to begin to purify thousands of sites of polluted groundwater. An EPA report estimated that it could cost between $900 million and $4.3 billion annually to implement one of the tools under the Clean Water Act for cleaning up the nation's waters.[93] It will require an integrated global effort of public and private groups, of individuals and corporations, to begin planning and implementing massive recycling, including agricultural, chemical, and other pollution controls to address water protection and control. Many companies have already begun conservation efforts. Xerox has halved its use of dichloromethane, a solvent used to make photoreceptors. The firm also reuses 97% of the solvent and will replace it with a nontoxic solvent. The Netherlands has a national goal of cutting wastes between 70% and 90%.

Causes of Environmental Pollution

Some of the most pervasive factors that have contributed to the depletion of resources and damage to the environment include:

1. *Consumer affluence*. Increased wealth—as measured by personal per capita income—has led to increased spending, consumption, and waste.
2. *Materialistic cultural values*. Values have evolved to emphasize consumption over conservation—a mentality that believes in "bigger is better," "me first," and a throwaway ethic.
3. *Urbanization*. Concentrations of people in cities increase pollution, as illustrated by Los Angeles, New York City, Mexico City, Sao Paulo, and Santiago, to name a few.
4. *Population explosion*. Population growth means more industrialization, product use, waste, and pollution.
5. *New and uncontrolled technologies*. Technologies are produced by firms that prioritize profits, convenience, and consumption over environmental protection. Although this belief system is changing, the environmental protection viewpoint is still not mainstream.
6. *Industrial activities*. Industrial activities that, as stated earlier, have emphasized depletion of natural resources and destructive uses of the environment for economic reasons have caused significant environmental decay.[94]

Enforcement of Environmental Laws

A number of governmental regulatory agencies have been created to develop and enforce policies and laws to protect the general and workplace environ-

ments. The Occupational Safety and Health Administration (OSHA), CPSC, EPA, and the Council on Environmental Quality (CEQ) are among the more active agencies that regulate environmental standards. The EPA, in particular, has been a leading organization in regulating environmental abuses by industrial firms.

In the 1970s, the EPA's mission and activities concentrated on controlling and decreasing toxic substances, radiation, air pollution, water pollution, solid waste (trash), and pesticides. The EPA has since used its regulatory powers to enforce several important environmental laws such as:

- *The Clean Air Act of 1970, 1977, 1989, and 1990:* The latest revision of this law includes provisions for regulating urban smog, greenhouse gas emissions, and acid rain, and for slowing ozone reduction. Alternative fuels were promoted and companies were authorized to sell or transfer their right to pollute within same-state boundaries—before, pollution rights could be bought, sold, managed, and brokered like securities.
- *The Federal Water Pollution Control Act of 1972:* Revised in 1977, this law controls the discharge of toxic pollutants into the water.
- *The Safe Drinking Water Act of 1974 and 1996:* Established national standards for drinking water.
- *The Toxic Substances Control Act of 1976:* Created a national policy on regulating, controlling, and banning toxic chemicals where necessary.
- *The Resource Conservation and Recovery Act (RCRA) of 1976:* This legislation provides guidelines for the identification, control, and regulation of hazardous wastes by companies and state governments. The $1.6 billion Superfund was created by Congress in 1980. It provides for the cleanup of chemical spills and toxic waste dumps. Chemical, petroleum, and oil firms' taxes help keep the Superfund going, along with U.S. Treasury funds and fees collected from pollution control. One in four U.S. residents lives within four miles of a Superfund site. It is estimated that 10,000 sites still need cleaning, and it may cost $1 trillion and take 50 years to complete this work.[95]
- *Chemical Safety Information, Site Security, and Fuels Regulatory Relief Act of 1999:* Created standards for storing flammable fuels and chemicals.

The Ethics of Ecology

Advocates of a new environmentalism argue that when the stakes approach the damage of the earth itself and human health and survival, the utilitarian ethic alone is an insufficient logic to justify continuing negligence and abuse of the earth. For example, Mark Sagoff argues that cost-benefit analysis can measure only desires, not beliefs. In support of corporate environmental policies, he asks, "Why should we think economic efficiency is an important goal? Why should we take wants and preferences more seriously than beliefs and opinions? Why should we base public policy on the model of a market

transaction rather than the model of a political debate? Economists as a rule do not recognize one other value, namely, justice or equality, and they speak, therefore, of a 'trade-off' between efficiency and our aesthetic and moral values. What about the trade-off between efficiency and dignity, efficiency and self-respect, efficiency and the magnificence of our natural heritage, efficiency, and the quality of life?"[96]

This line of reasoning raises questions such as these: What is a "fair market" price or replacement value for Lake Erie? The Atlantic Ocean? The Brazilian rainforest? The stratosphere?

Five arguments from those who advocate corporate social responsibility from an ecology-based organizational ethic include the following:

1. Organizations' responsibilities go beyond the production of goods and services at a profit.
2. These responsibilities involve helping to solve important social problems, especially those they have helped create.
3. Corporations have a broader constituency than stockholders alone.
4. Corporations have impacts that go beyond simple marketplace transactions.
5. Corporations serve a wider range of human values than just economics.[97]

Although these guidelines serve as an ethical basis for understanding corporate responsibility for the environment, utilitarian logic and cost-benefit methods will continue to play key roles in corporate decisions regarding their uses of the environment. Also, judges, courts, and juries will use cost-benefit analysis in trying to decide who should pay and how much when settling case-by-case environmental disputes. Some experts and industry spokespersons argue that the costs of further controlling pollutants such as smog outweigh the benefits. For example, it is estimated that the cost of controlling pollution in the United States has exceeded $160 billion. It costs the EPA $7 billion a year to regulate air pollution, and the benefits range from $19 billion to $167 billion.[98] A WHO study has estimated that air pollution will cause 8 million deaths worldwide by 2020. How many lives would justify spending $160 billion annually? Although some benefits of controlling pollution have been identified, such as the drop in emissions, improvement of air and water quality, cleanup of many waste sites, and growth of industries and jobs related to pollution control (environmental products, tourism, fishing, and boating), it is not clear whether these benefits outweigh the costs.[99] One question sometimes asked regarding this issue is: Would the environment be better off *without* the environmental laws and protection agencies paid by tax dollars?

Green Marketing, Environmental Justice, and Industrial Ecology

An innovative trend in new ecology ethical thinking is linking the concepts of green marketing, environmental justice, and industrial ecology.[100] Green mar-

keting is the practice of "adopting resource conserving and environmentally-friendly strategies in all stages of the value chain."[101] The green market was estimated at 52 million households in the United States in 1995. One study identified trends among consumers who would switch products to green brands: 88% of consumers surveyed in Germany said they would switch, as would 84% in Italy, and 82% in Spain. Nearly 70% of respondents across the globe said they were somewhat to very willing to spend more on a green product, compared to the same product without green features. Only 11% of respondents were not willing at all to spend more money for green features. In open-ended comments, many analysts noted that the recession heavily influences their buying decisions at the current time, and cutting costs seems more important to the average consumer than purchasing green products. Respondents would, however, buy green products if the price were not significantly higher.

In write-in responses, some respondents expressed concern that green products are not necessarily healthier or better for the environment, even though they claim to be. According to one respondent from the EU, "It's sometimes hard to know how much of that is just marketing and how sustainable green products are in the longer term rather than just being good to someone's conscience."[102] Companies are adopting green marketing as a competitive advantage and are also using green marketing in their operations. For example, packaging materials that are recyclable, pollution-free production processes, pesticide-free farming, and natural fertilizers.

Environmental justice is "the pursuit without discrimination based on race, ethnicity, and/or socioeconomic status concerning both the enforcement of existing environmental laws and regulations and the reformation of public health policy."[103] Linking environmental justice to green marketing involves identifying companies that would qualify for visible, prestigious awards—such as the Edison Award—for producing the best green products. To win the award, companies need to demonstrate that they had, for example, (1) produced new products and product extensions that represented an important achievement in reducing environmental impact, (2) indicated where and how they had disposed of industrial and toxic materials, and (3) incorporated recycling and use of less toxic materials in their strategies and processes.

The green marketing and environmental justice link to industrial ecology is made in the long-range vision and practice of companies' integrating environmental justice into sustainable operational practices on an industry-wide basis. Industrial ecology is based on the principle of operating within nature's domain—that is, nothing is wasted; everything is recycled.

Rights of Future Generations and Right to a Livable Environment

The ethical principles of rights and duties regarding the treatment of the environment and multiple stakeholders are (1) the rights of future generations and (2) the right to a livable environment. These rights are based on the responsibility that the present generation should bear regarding the preservation of the environment for future generations. In other words, how much of

the environment can a present generation use or destroy to advance its own economic welfare? According to ethicist John Rawls, "Justice requires that we hand over to our immediate successors a world that is not in worse condition than the one we received from our ancestors."[104]

The right to a livable environment is an issue advanced by William T. Blackstone.[105] The logic is that each human being has a moral and legal right to a decent, livable environment. This "environmental right" supersedes individuals' legal property rights and is based on the belief that human life is not possible without a livable environment. Therefore, laws must enforce the protection of the environment based on human survival. Several landmark laws have been passed, as noted earlier, that are based more on the logic related to Blackstone's "environmental right" than on a utilitarian ethic.

Recommendations to Managers

Boards of directors, business leaders, managers, and professionals should ask four questions regarding their actual operations and responsibility toward the environment:

1. How much is your company really worth? (This question refers to the contingent liability a firm may have to assume depending on its practices.)
2. Have you made environmental risk analysis an integral part of your strategic planning process?
3. Does your information system "look out for" environmental problems?
4. Have you made it clear to your officers and employees that strict adherence to environmental safeguarding and sustainability requirements are a fundamental tenet of company policy?[106]

Using the answers to these questions, an organization can determine its stage on the corporate environmental responsibility profile. The stages range from Beginner (who show no involvement and minimal resource commitment to responsible environmental management) to Proactivist (who is actively committed and involved in funding environmental management).

Finally, managers and professionals can determine whether their company's environmental values are reflected in the following ethical principles presented in R. Edward Freeman and Joel Reichart's article, "Toward a Life Centered Ethic for Business."[107]

The Principle of Connectedness. Human life is biologically dependent on other forms of life, and on ecosystems as a whole, including the nonliving aspects of ecosystems. Therefore, humans must establish some connection with life and respect that it exists because living things exist in some state of cooperation and coexistence.

The Principle of Ecologizing Values. Life exists in part because of the ecologizing values of linkage, diversity, homeostatic succession, and community. There is a presumption that these values are primary goods to be conserved.

The Principle of Limited Competition. "You may compete [with other living beings] to the full extent of your abilities, but you may not hunt down your competitors or destroy their food or deny them access to food. You may compete but may not wage war." (We would add to the last sentence, "without just cause.")[108]

Chapter Summary

The ethical principles related to corporate responsibility toward consumers include: (1) the duty to inform consumers truthfully; (2) the duty not to misrepresent or withhold information; (3) the duty not to unreasonably force consumer choice or take undue advantage of consumers through fear or stress; and (4) the duty to take "due care" to prevent any foreseeable injuries. The use of a utilitarian ethic was discussed to show the problems in holding corporations accountable for product risks and injuries beyond their control. These principles continue to apply in contemporary advertising online, through cell phones, and media.

Businesses have legal and moral obligations to provide their consumers with safe products without using false advertising and without doing harm to the environment. The complexities and controversies with respect to this obligation stem from attempts to define "safety," "truth in advertising," and levels of "harm" caused to the environment. The Federal Trade Commission's guidelines for online marketing show that this agency has considerable power and legitimacy in informing the public about ads; it also serves as a useful watchdog on corporate advertising and product regulation. Arguments for and against advertising were presented, with problematic examples of false advertising from the food and tobacco industries highlighted.

Product safety and liability were discussed through the doctrines of negligence, strict liability, and absolute liability. The legal and moral limits of product liability were summarized. States are now moving to limit punitive damages in product liability cases, and tort reform is predicted to change the direction of product liability litigation toward more protection for manufacturers than for injured consumers.

Corporate responsibility toward the environment was presented by showing how air, water, and land pollution is a serious, long-term problem. Federal laws aimed at protecting the environment were summarized. Increasing concern over the destruction of the ozone layer, the destruction of the rain forests, and other environmental issues has presented firms with another area where economic and social responsibilities must be balanced. Innovative concepts and corporate attitude changes were discussed. Green marketing, environmental justice, and industrial ecology principles are being practiced by a growing number of corporations, particularly in Europe—especially since green products and clean manufacturing processes (and certifications) offer a competitive advantage. An innovative move by some corporations is to include environmental safety practices in the strategic, enterprise, and

supply-chain dimensions of industrial activities and practices. A diagnostic enables a company to identify its stage of social responsibility toward the environment.

Questions

1. What advertisements—and where do these appear (TV, Internet, print)—do you find "unethical" but legal? Explain.
2. What ethical principles of advertising apply to consumers in all cultures and countries? Explain.
3. Identify some problems associated with the free-market theory of corporate responsibility (discussed in Chapter 4) for consumers? Compare this view with the social contract and stakeholder perspectives (also discussed in Chapter 4) of corporate social responsibility.
4. Where does the liability of a company end and the responsibility of consumers begin for products? Explain your answer as you define this question more specifically.
5. What constitutes "unreasonable risk" concerning the safety of a product? Identify considerations that define the safety of a product from an ethical perspective.
6. Do you believe the environment is in trouble from climate change and global warming, or do you believe this is "hype" from the press and scientists? Explain.
7. Evaluate and comment on this statement: "North American and European countries have created waste, pollution, and environmental devastation for decades, even centuries. Is it fair that countries like China and India should have the same sanctions now regarding their use of technologies, fuels, and other polluting devices as North America and Europe?"

Exercises

1. Identify a recent example of a corporation accused of false or deceitful advertising. How did it justify the claims made in its ad? Do you agree or disagree with the claims? Explain.
2. In a paragraph, explain your opinion of whether the advertising industry requires regulation.
3. Can you think of an instance when you or someone you know was affected by corporate negligence in terms of product safety standards? If so, did you or the person communicate the problem to the company? Was any action taken regarding the defective product? Explain.
4. Do you believe cigarette, cigar, and pipe smoking should be banned from all public places where passive smoking can affect nonsmokers? Explain. Use the following (or other) web sites to argue your position: http://www.cdc.gov; http://www.tobacco.org; http://www.thetruth.com; http://www.trytostop.org; http://www.cancer.org; http://www.getoutraged.com.

5. Find a recent article discussing the environmental damage caused by a corporation's activities. Recommend methods the firm in the article should employ to reduce harmful effects on the environment.
6. Find a recent article discussing an innovative way in which a corporation is helping the environment. Explain why the method is innovative and whether you believe the method will really help the environment or will only help the company promote its image as a good citizen.

Real-Time Ethical Dilemma

Questionable Conflict of Interest

I am a project manager who supports corporate-citizenship-funded programs for our large insurance company. I am responsible for helping choose proposals to support for environmental, community education, and alumni related projects. Last year, the division in which I work facilitated 120 sponsorships, engaged 100 employees, and provided nearly 25 speakers to various programs.

We have a set of criteria to guide our decision-making process and to help proposals that demonstrate real need. This focus aligns with the mission of the company. Still, there are many organizations with proposals that are high profile, legacy, and/or ones also supported by executives at our firm. These executive-backed requests sometimes receive preferential treatment over the requests that do meet our needs criteria. Several individuals and groups in the company who are aware of these exceptions either shrug it off or feel comfortably conflicted.

Executives form close ties with some of the groups who receive funding without going through our formal process. A dilemma our group faced last year occurred when one executive pressured us to fund a nonprofit that his sister founded. It was a small nonprofit with an environmental focus in an unassigned area and community in which our Program operates. Since this is not the only time executives have bypassed our company policy, it is one that smacked of nepotism!

While I hesitate to judge whether or not this particular executive was right or wrong, I continue to have issues with the assumed power and authority that executives in our firm take to trump our mandated mission and decisions with regard to funding needy programs. What more should I have done (should I do) to stand up for my personal and professional beliefs?

My reasoning to execute the sponsorship of that particular program was because I was afraid of the backlash if I did not act. The organization has created a culture where this is acceptable and even though I am not comfortable with this part of our culture, I cannot do much to change it at this point. I cringe at this particular situation and others since I was raised with an ethic of fairness and acting justly toward others. If all people cannot act in a certain way, then no one should act that way. It is difficult managing this process in the real world because people and organizations inevitably have competing interests, stakes, and power in the hierarchy of a company.

Questions

1. What exactly is the conflict of interest here?
2. Is this a serious conflict of interest or just a "business as usual" situation? Explain.
3. What would you have done in this situation before the executive took a decision to fund the sister's program if you had been this project manager? Explain.
4. Describe the ethical principles (or reasoning) you used in your answer to question 3.

Cases

Case 12

For-Profit Universities: Opportunities, Issues, and Promises

Background

For-profit colleges and universities, compared to their public institutional counterparts, are governed and operated by private corporations. Enrollment in for-profit institutions over the past 20 years has increased 225%, taking in approximately 12% of all postsecondary students–2.4 million as of the 2010–2011 academic year. Estimates for 2013 indicate that the top 50 for-profit colleges and universities headcount totals over 1,260,000. Because public community colleges, or many private universities, cannot meet this level of demand from primarily working adults, part-time students, and working parents with students, for-profit institutions provide an option for those who would otherwise not be able to receive a college education.

Competitive advantages of for-profit institutions include "flexible scheduling with year-round enrollment, online options, small class sizes and convenient locations." These characteristics attract a large and growing student population entering the education market. It seems the entrepreneurial wave of for-profits has and continues to serve a niche that traditional universities and institutions of higher learning have not served, and perhaps cannot serve, at least to date.

Trouble in Paradise

For-profit higher education universities and colleges have entered the eye of the storm on Capitol Hill over the last few years with regard to questionable recruiting practices and use of taxpayer funds that have not resulted in gainful employment and promised results for many students. Although for-profit universities have garnered the favor of Wall Street investors and have formed a powerful lobbying group to promote for-profit interests, questions continue to surface as the boundaries between traditional academia and the business of higher education blur.

Congressional Investigation

The 2012 report of a two-year investigation into for-profit colleges by the U.S. Senate's Health, Education, Labor, and Pensions Committee, comprised primarily of Democratic Party legislators, revealed staggering statistics that have resulted in intense scrutiny by the federal government, creating a call to action for regulation to monitor for-profit institutions. According to other recent investigations, currently "more than $30 billion in taxpayer funds flow to the [for-profit] schools each year" and "about 60% of for-profit colleges receive over 70% of their revenue from U.S. government programs." These statistics, combined with some for-profit student testimonies about the "dishonest" and "fraudulent" practices of their educational institutions, have resulted in lawsuits. One such lawsuit

reached settlement on July 26, 2013, after a "for-profit college in Richmond, Va., agreed to pay $5 million in a class-action settlement filed by eight former students, who argued that the training/education they received was a sham."

Senator Tom Harkin of Iowa led the investigation into for-profit schools and stated that "in this report, you will find overwhelming documentation of exorbitant tuition, aggressive recruiting practices, abysmal student outcomes, taxpayer dollars spent on marketing and pocketed as profit, and regulatory evasion and manipulation." He added that "These practices are not the exception—they are the norm. They are systemic throughout the industry, with very few individual exceptions."

The storm has continued to build since 2010 as the pressures for legislation increased, driven by senate investigations, increasing litigation, and courts setting precedents. For-profit education probes began in 2010 when press reports started to "raise questions about the quality of proprietary institutions." "These questions stem from the rapid growth of this industry over the last few years, reported aggressive recruitment of students by such institutions, increased variety in the delivery methods used to provide education to students, and the value of the education provided by such institutions."

College, Inc., PBS, and For-Profit Universities

A Public Broadcasting Service (PBS) documentary filmed in 2010 named *College, Inc.* profiled the for-profit college industry, its historical roots, certain business practices, investors' interests, and issues surrounding the industry. The film examined the application of "private sector principles" to the education industry. The documentary's profile of Michael K. Clifford, a pioneer for-profit education investor and deal-maker, provided a lens to view for-profit education as an opportunity for investors to both realize a financial return on their investment, while also achieving so-called philanthropic goals; that is, helping failing U.S. universities and colleges keep their doors open for students. (One of his specialties is buying faltering private U.S. colleges).

Bringing a combination of what Clifford calls the "Three M's: Money, Management, and Marketing," investors have been able to turn around some of the failing institutions and leverage significant value-adds, such as accreditations, while helping the universities bring in huge profits using an improved profit business model. Although there are concerns about the for-profits' "business model," the PBS documentary points out that "'Nonprofit' colleges which pay their leaders executive salaries while operating multi-billion dollar sports franchises have long since ceded the moral high ground when it comes to chasing the bottom line."

Pressures on the For-Profit Sector

These external probes have jolted some in the for-profit educational sector as facts from the investigation and large monetary settlements are highlighted by the media. For-profit supporters, however, continue to focus on the impetus of

creating these needed institutions, asserting that they "provide very necessary services for rural people and for people learning certain trades" and primarily "help accommodate the mushrooming demand for higher education." Political supporters, many of whom are Republicans, continue to point out the advantages of for-profit education out of concern about the regulatory legislative framework proposed by the Obama administration that emphasizes the "need to look for ways to improve the bad players, but not cast a wide net over the industry."

Key Issues

The for-profit higher education sector's growth and controversy over its business model and practices have triggered reaction and questioning at the state and federal government levels. Some of the primary issues include: the quality of education of these institutions; the amount of money in scholarships and loans they receive from the federal and state governments; the recruiting tactics they use to attract students; and the failure of their graduates in finding jobs.

The National Conference of State Legislatures noted that "Critics of for-profit institutions argue that many schools and programs leave students with large amounts of debt, few employable skills, and at a greater risk of not completing a degree at all. This is of greater concern because of the heavy federal subsidies that for-profit institutions receive. . . . Lawmakers have begun to look for ways to better hold these schools accountable for graduating students that can find gainful employment, not be overburdened with large debt they are unable to pay back, and in this way ensure taxpayers are getting a good return on their investment." A key concern regarding for-profits' business practices stems from the previously quoted statistics that said "more than $30 billion in taxpayer funds flow to the schools each year" and "about 60% of for-profit colleges receive more than 70% of their revenue from U.S. government programs." The industry seems fundamentally subsidized by public taxpayers who are the source of the money for these loans. As a consequence, a nervous climate of uneasiness has developed that reflects the same concerns that preceded the recent U.S. subprime lending and housing crisis.

A June 24, 2010, *New York Times* article titled "Battle Lines Drawn Over For-Profit Colleges" pointed out that "one source of contention was the planned appearance at the hearings of Steven Eisman, a hedge fund manager known for having predicted the housing market crash. He has recently compared the for-profit college sector to the subprime mortgage banking industry—arguing that both grew rapidly based on lending to low-income people with little ability to repay the loans." For-profit schools make up nearly half of all student defaults. For-profit schools claim to give students who have been turned away from other institutions the opportunity of a higher education, but the reality is that the wider net they have cast primarily includes lower-income individuals who do not have the propensity to be able to pay back these loans, therefore creating an effective "house of cards" and a predicted "student loan bubble."

Statistics from the U.S. Department of Education also showed that for the Fiscal Year (FY) 2011 two-year and official FY 2010 three-year period, "For-profit institutions continue to have the highest average two- and three-year cohort default rates at 13.6 percent and 21.8 percent, respectively. Public institutions followed at 9.6 percent for the two-year rate and 13 percent for the three-year rate. Private non-profit institutions had the lowest rates at 5.2 percent for the two-year rate and 8.2 percent for the three-year rate." In addition, "the average tuition at for-profit colleges is $14,000 a year, compared with $2,500 at community college and $7,000 in-state tuition at a public four-year college, the report found. . . . Students take out larger loans—and default more often." Given the current economic conditions, "with costs soaring, incomes stagnating and little help from government; it was not surprising that total student debt, around $1 trillion, surpassed total credit-card debt last year." The findings of the for-profit universities investigations are pressuring states to increase monitoring of those institutions. State legislatures in Connecticut, California, Michigan, Delaware, and Maryland have already implemented criteria related to such monitoring.

Concluding Comments

It is in the interests of states and the federal government to effectively but fairly regulate for- and not-for-profit higher education institutions for all stakeholders. With regard to this case, it is also in the interests of for-profit universities and colleges to legally and ethically attract and recruit students, as well as charge rates similar to comparable competitors, and to produce graduating students who can find gainful employment given their education, skills, and abilities. The role of both the federal and state legislatures is to provide "safeguards and transparency for students, hold schools accountable for providing meaningful degrees, and evaluate allocation of state student aid."

How and in what ways for-profits will fit into the mix of a changing education landscape in the United States and internationally remains to be seen—especially given the rise of massive online open curriculum (MOOC) initiatives, rising student debt at all higher educational institutions, and the need for different types of jobs and skills in this century.

Questions for Discussion

1. What are the main issues in this case with the for-profit higher university and college education sector?
2. Watch the online video *College, Inc*. produced by PBS. Evaluate PBS's role in making the vide*o and* its content. Is this a fair, objective account of for-profits? Why? If not, what information is needed in the video? Explain your reasoning.
3. Identify some of the major stakeholders and issues using your answers and findings in the above questions, and this case. After reviewing the major stakeholders' interests, arguments, and facts regarding these issues, what did you discover? What and whose arguments and information did you find most compelling to help resolve the controversy? Where do you now stand and why on for-profit university institutions and practices? Explain.

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Case 13

Fracking: Drilling for Disaster?

In a lively 2013 CNN article, "Fears of Quakes and Flammable Tap Water Hit Britain as Fracking Looms," Dan Rivers and Ben Brumfield write, "The fear of fracking has come to Britain, replete with worries about potential earthquakes and tap water tainted with natural gas that bursts into flames at the strike of a match." The lifting in May 2013 of a ban on extracting (drilling) for natural gas found in rock layers deep underground in the town of Balcombe in southern England has several hundred protesters worried. Perhaps they have seen the American documentary *Gasland II* (2013) by Josh Fox, which shows several American homeowners losing the value of their properties and homes to certain energy corporations' drilling and releasing flammable gas in their kitchen sinks.

The debate over this drilling process in the United States and now in England has proponents and opponents stating their claims and arguing for very large stakes. Opponents fear for their homes and property values and potentially may have to leave their residences (many already have) because of the aftereffects and devastation caused. Proponents, including President Obama, see natural gas on U.S. soil as an energy-independent national strategy. Cuadrilla, the British energy company waiting to drill in Balcombe, "believes there is about 200 trillion cubic feet of gas under the ground just within one of its local license areas. To put that figure into context, the United Kingdom uses about 3 trillion cubic feet of gas a year."

What Is Fracking?

Hydraulic fracturing or "fracking" is a process used to retrieve natural gas that is otherwise inaccessible. This technology was first developed in the late 1940s and involves pumping a mixture of water, sand, and chemicals—the "fracking fluid"—deep underground to break up shale rock formations and release pockets of gas. Fracking usually occurs when a new well is drilled, but wells may be fractured multiple times to increase gas extraction. In its lifetime, a well can be fracked up to 18 times; 90% of all oil and gas wells in the United States are "fracked" to boost productivity, according to the Interstate Oil and Gas Commission.

First, a well is drilled until it nears the shale layer, typically 5,000 to 12,000 feet below ground. The bore then changes direction and continues drilling horizontally. After the drill is removed, production casing is inserted, and cement is pumped through and around the casing. The cement is installed to prevent anything from getting into the fresh water aquifers. Explosive charges then puncture the casing and cement on the horizontal portion of the drilled tunnel. A mixture of water, sand, and chemicals is pumped down the well and out of these apertures at high pressures. The fracking fluid is over 99% water, but contains over 500 different chemicals. As a result, a single "frack job" can require as much as 5 million gallons of water. The mixture fractures the rock and allows the trapped gas to escape into the well bore.

The fracking process not only requires millions of gallons of water but also results in large amounts of toxic waste. Some wastewater comes back up the well and must be collected. This wastewater contains dissolved solids such as sulfates and chlorides, metals, and other potentially hazardous components. Conventional municipal sewage or drinking water treatment plants cannot remove the sulfates and chlorides. Instead, the fracking fluid must be sent to a treatment plant, injected into underground disposal wells, or mixed with fresh water and reused.

Benefits

Experts have known for years that natural gas deposits existed in deep shale formations, but until recently the vast quantities of natural gas in these formations were not thought to be recoverable. Hydraulic fracturing makes the drilling process more efficient and makes available vast new reserves of natural gas across the country. Natural gas plays a key role in meeting the United States' energy demands, supplying about 22% of the total. The Energy Information Administration estimates that there is more than 1,744 trillion cubic feet of technically recoverable natural gas that exists within the United States, 60% of which is contained as shale gas, tight sands, and coaled methane. The total amount of this resource is estimated to be able to provide enough natural gas to the United States for the next 90 years. Separate estimates of the shale gas resource extend this supply to 116 years.

Shale formations in the United States containing large quantities of natural gas are concentrated in the Northeast Appalachian range and the Rocky Mountain range of the West. The Marcellus Shale formation, which extends from West Virginia and eastern Ohio through Pennsylvania and into southern New York, could become one of the world's most productive natural gas fields. It is estimated that this area alone possesses 500 trillion cubic feet of gas or more, enough to supply the entire East Coast for 50 years. The majority of "fraccidents" have taken place across Pennsylvania in this Marcellus Shale formation, potentially compromising the Delaware River, Monongahela River, and Susquehanna Rivers. With the help of fracking, natural gas currently satisfies nearly one-quarter of the nation's power needs. At current drilling rates and consumption levels, it's expected to provide more than half the nation's natural gas by 2030, according to an MIT study.

President of the American Chemistry Council (ACC), Cal Dooley states, "One of our highest priorities in this country is to establish energy security and to reduce our dependence on imported oil. . . . We see a game-changer here with our ability to capitalize on what is estimated to be a 100-year supply of natural gas in shale deposits." This abundant domestic supply of natural gas has provided the United States with a competitive edge in overseas markets and a source for consumption within the country.

Sara Banaszak, senior economist for the American Petroleum Institute (API) further states, "Developing domestic supplies of natural gas will mean billions of dollars in government revenue and reductions in greenhouse gas emissions."

The industry boasts that gas is cleaner than oil or coal, emitting less pollution when burned. In May 2010, an industry-financed study conducted at Pennsylvania State University estimated that gas companies spent $4.5 billion developing the Marcellus Shale formation in Pennsylvania. As a result, it has generated $389 million in state and local tax revenue and more than 44,000 jobs.

Instant Millionaires

The natural gas boom in the United States has resulted in big businesses compensating local individuals for the use of their land to drill. Money is earned in signing bonuses, as well as royalties from the amount of gas extracted. Other landowners cashed in by leasing their mineral rights and allowing gas companies to drill horizontally under their properties. One company, Chesapeake Energy, claims to have contracted with a million American households. This modern-day gold rush has enabled struggling locals to become practically millionaires overnight.

Homeowners are offered anywhere from $350 to $30,000 an acre. With additional royalties, this can be a very tempting offer. Rowena Shager of Louisiana negotiated to lease her land. Within a short time, fracking fluid had polluted her family's drinking water. She states, "If I thought I was putting my family's life in jeopardy, or taking away from the value of my property, I never would have signed." A significant number of families are unaware of the potential risks involved when signing contracts with natural gas companies and have suffered negative consequences as a result.

Environmental and Health Concerns

The fracking process has received significant attention in the threats it poses to the environment and human health, particularly water and air pollution across the country. Regulators say that flushing too much of this wastewater into a river could severely harm animals. In 2009, 16 cattle dropped dead near a Chesapeake Energy drilling site in Louisiana after drinking from a mysterious fluid used by drillers that had flooded off during a storm.

Fracking has also been responsible for well-water contamination, filling a basement with methane and blowing up a house in Ohio, and poisoning 17 crows in Louisiana, according to a statement from U.S. environmental group Sierra Club. Nonprofit organization Natural Resources Defense Council (NRDC) warns that fracking could also trigger earthquakes in certain areas.

The industry maintains its position that hydraulic fracturing has been safe for decades, yet homeowners are coming forward with an entirely different story. Because fracking takes place thousands of feet below the water table where groundwater settles, local drinking water is at risk for contamination. Residents in six states have documented more than 1,000 cases of water contamination as a result of hydraulic fracturing. In the documentary *Gasland* (2010), Josh Fox travels across the country meeting families that have been affected by hydraulic fracturing. From these interviews, there is evidence that drinking contaminated

water has caused headaches, brain damage, asthma, cancer, arsenic poisoning, and loss of taste and smell.

The small town of Dimock, Pennsylvania, is at the heart of the drilling debate. Cabot Oil drilled over 40 wells in just a few months. Gas then contaminated local drinking wells, making the water so hazardous that families are able to ignite their drinking water and start a fire. In late 2009, a group of 19 Dimock residents sued Cabot in federal court for contaminating their wells and devaluing their real estate. The case was finally settled in December 2010, with Cabot Oil and Gas Corporation agreeing to pay $4.1 million to the families affected by methane contamination attributed to faulty Cabot natural gas wells. The settlement also requires Cabot to offer and pay to install whole-house gas mitigation devices in each of the affected homes. Once the terms of the agreement have been met, Cabot plans to resume operations in Dimock.

Environmental Protection Agency (EPA)

A 2004 hydraulic fracturing study by the EPA found no evidence of water-table contamination. The study concluded that 80% of the chemicals degrade underground or are recovered. Due to criticisms of the study, as well as increased attention on fracking, the agency has recently begun a new two-year study of hydraulic fracturing. In March 2012, the EPA released test results concluding that Dimock's water contamination does not pose any risk to human health. The arsenic levels were deemed safe; however, the water of six homes did contain sodium, methane, chromium, and bacteria. Many residents have lost all trust in their drinking water and say they will never use it again. The EPA is continuing its tests of Dimock homes' drinking water.

It has asked nine natural gas services providers to voluntarily disclose data on chemicals used in hydraulic fracturing. These gas companies include BJ Services, Complete Production Services, Halliburton, Key Energy Services, Patterson-UTI, PRC, Inc., Schlumberger, Superior Well Services, and Weatherford. The EPA intends to use this data in this study underway to determine whether fracking has an impact on water quality for residents living in the vicinity. By November 2010, Halliburton was the only company that refused to voluntarily submit data. As a result, the EPA has issued a subpoena to Halliburton in order to gain this information.

Congress and Regulation

Congress enacted the Clean Water Act in 1972 and the Safe Drinking Water Act in 1974, giving the EPA the power to set national standards regarding maximum acceptable levels of water-contaminates in public water systems. The Safe Drinking Water Act also authorizes states to create regulations to protect their underground drinking water sources, as long as each state complies with the EPA's minimum requirements and receives EPA approval.

The George W. Bush administration introduced the Energy Policy Act (EPACT) of 2005 that exempted oil and gas companies from certain federal

regulations protecting drinking water, amending the Safe Drinking Water Act. Bush's vice president Dick Cheney was chairman and CEO of Halliburton Corporation from 1995 to 2000. His former employment and strong ties to the gas and drilling industry certainly influenced the legislation.

EPACT changed the definition of "underground injection" to exclude "the underground injection of fluids or propping agents (other than diesel fuels) pursuant to hydraulic fracturing operations." This amendment, which came to be known as the "Halliburton Loophole," exempted fracking from federal law and gave jurisdiction and authority over hydraulic fracturing operations to the states. Meanwhile, most state oil and gas regulatory agencies do not require companies to report the volumes or names of chemicals being used in extraction. According to the nonprofit Oil and Gas Accountability Project, one of the country's dirtiest industries enjoys the exclusive right to "inject toxic fluids directly into good quality groundwater without oversight." This is a significant issue because Americans get approximately half of all drinking water from underground sources.

In 2009, U.S. Representative Diane Degette (Democrat, Colorado) introduced a bill called the Fracturing Responsibility and Awareness to Chemical Act (FRAC Act). Under this bill, gas producers would be required to disclose chemical identities of all constituents of the fracturing fluid, making this information available on a web site.

This would allow emergency crews and first responders to have access to the chemical identities in the case of an emergency. The bill would also close the Halliburton Loophole. As of 2013, Congress has not passed this bill.

State Legislation

More than 30 states have varying degrees of shale production or exploration. A significant number of states' legislation is based on rules laid down by Colorado following many stakeholder discussions. After documented damage from fracking within the state, Colorado implemented a comprehensive drilling plan including: practices to minimize the negative effects on communities and the environment; drilling at a required distance from homes; and reporting chemical identities.

Drilling in the Northeast is the most recent, while hydraulic fracturing operations in the southern and western areas of the country are much more established. Drilling into the Marcellus Shale formation has spurred up controversy and resistance. Pennsylvania passed regulations on fracking in November 2010, requiring disclosure of a Material Safety Data Sheet with a list of additives used in drilling. In December 2010, New York tried to place a temporary ban on fracking until May 2011, in order to study environmental impacts. Governor David Paterson vetoed the bill, stating that it would put many people out of work. Instead, he issued an executive order instituting a moratorium that extended until July 1, 2011, beyond the date specified in the original bill. Oil companies are pleased because this executive order makes a distinction between the types of drilling, allowing horizontal drilling but disallowing vertical. Recently the cities of Pitts-

burg, Pennsylvania, and Buffalo, New York, have enacted altogether bans on hydraulic fracturing.

New York State will possibly not be allowing fracking anytime soon, with drilling giant Chesapeake Energy reportedly abandoning its fight to retain land leases in portions of the state sitting atop vast natural gas reserves. "We can't speak to what drove Chesapeake's decision. However, it's fundamental that organizations prioritize their resources and make decisions based on the known business climate. They do not embrace uncertainty," said Jim Smith, spokesman for the Independent Oil and Gas Association of New York.

Questions for Discussion

1. Do you think U.S. self-dependence on natural gas is worth the contamination of water supplies?
2. Should fracking be allowed to continue given the risks and damage to the environment? Why or why not?
3. If you were a top executive at Chesapeake Energy or Cabot Oil, for example, how would you persuade homeowners to sell your company the use of their land for drilling? How would your personal and corporate ethics guide you?
4. What role does legislation play in holding fracking companies accountable to ethical behavior?
5. In your opinion, how should fracking companies respond to the new EPA study regarding hydraulic fracturing?

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Case 14

Neuromarketing

Background Information

Contemporary consumers have access to millions of products. The days when a consumer entered a store looking for a pair of sneakers and had only two options are over. First, markets have expanded to online as well as physical locations. Secondly, markets are now saturated with different brands, pricing, and payment options—all competing for consumers' attention. A present challenge for marketers is to determine what consumers want, need, and are likely to buy—both online and in physical locations.

Since almost 90% of consumer purchasing decisions take place at what can be considered an "unconscious" or perhaps "subconscious" level, it has not always been easy to accurately identify the drivers of consumers' buying behaviors—until now. *Neuromarketing* is a recent phenomenon that takes this observation into consideration to develop marketing strategies corporations can use. The term neuromarketing was coined in 2002 by professor Ale Smidts and refers to a practice that combines neuroscience and marketing to delve into the unconscious minds of consumers.

Neuromarketing technology provides a starting point to understand how consumers react to marketing stimuli, how they make their decisions, and what moves them from a potential customer to a buyer. The application of neuroscience can result in "a better identification and understanding of the cerebral mechanism that fundament the consumer's behavior."

A main tool used in neuromarketing is functional magnetic resonance imaging (fMRI). fMRI is a technology that allows tracking the brain's responses when exposed to different stimuli. Using an fMRI, brain activity can be recorded noninvasively, without any risks of radiation. Another available technology to neuromarketers is the electroencephalogram (EEG) test. EEG tests measure electrical activity within the brain and can be utilized with software to produce several different views of the brain. EEG tests use flashes of red and yellow to show which area of the brain is engaged by the stimuli. This is considerably useful to researchers and marketers, given that each different part of the brain correlates with a different function. In addition to fMRI and EEG tests, neuromarketing also encompasses eye-tracking and galvanic skin response (GSR) tests. Eye-tracking technology can determine exactly where a person is looking; it allows for the monitoring of pupil movement. The technology allows marketers to determine if users are having trouble locating information or navigating through a web page, or if they are failing to see information altogether. GSR tests, on the other hand, measure the degree of electrical conductance across the surface of skin and can indicate emotional responses.

Since neuromarketing has increased in popularity, several companies have become frontrunners in the market. NeuroFocus, with a team of neuroscience and marketing experts from U.C. Berkeley, MIT, Harvard, and Hebrew University,

is one of the market leaders. The company has recently been backed by the Nielsen Company, a worldwide leader in marketing and advertising research and have numerous Fortune 100 clients ranging from automobile manufacturers to consumer packaged goods, as well as major cable television and motion picture industries.

EmSense, another neuromarketing vendor, combines neuroscience experts from MIT, Harvard, and Stanford with marketing experience from Pepsi-Cola, Disney, and Gillette. Like NeuroFocus, EmSense has worked with large companies like Microsoft. NeuroFocus' portfolio offers solutions for advertising, in-store, videogame, packaging and online marketing elements. Sands Research is a company that offers neuroscience-based research. In addition to using technology like EEG tests and eye tracking, Sands has worked to develop its own system of scoring media, the Neuro Engagement Factor (NEF). The NEF ranks marketing elements, like advertisements, on a scale of 1 to 5 based on the level of consumer engagement. The company's technology has attracted clients like Sam's Club and Chevron and has also allowed it to conduct insightful studies on Super Bowl advertisements.

Another company that incorporates neuromarketing insights and related methods into its strategy is Hyundai. Hyundai recently employed the use of EEG technology to test consumer reactions to a new 2011 test model. Using a test group of 15 men and 15 women, Hyundai asked participants to stare at different parts of the model, while monitoring the electrical activity in their brains. A manager of brand strategy, Dean Macko, stated, "We want to know what consumers think about a car before we start manufacturing thousands of them." Macko expects the company to make adjustments to the model's exterior based on the EEG reports.

The Weather Channel (TWC) has also chosen to utilize neuroscience. In this case, TWC was looking to optimize its on-air promotions for one of its series, "When Weather Changed History." To do this, the company teamed up with NeuroFocus and utilized three different neuroscience technologies for the study: EEG tests, eye-tracking technology, and GSR. These methods tested viewers' neurological and biophysical responses to three different promotions. The study was aimed at answering four different questions: "Are the spots effective? What about each of them is more or less effective? How well do they convey the intended messages? How do we build the most effective final versions of the spots?" To answer these questions, NeuroFocus measured metrics like attention, emotional engagement, and memory retention. Each spot was scored based on these metrics, providing valuable insights: "TWC's marketing team welcomed this research, because the information was clear, intuitive, quantitative, and objective. It was also well received because it helped pinpoint how we could improve the effectiveness of our promos."

Uma Karmarkar cites the example of junk-food giant Frito-Lay, which in 2008 hired a neuromarketing firm to look into how consumers respond to Cheetos, the top-selling brand of cheese puffs in the United States. Using EEG technology on a group of willing subjects, the firm determined that consumers respond

strongly to the fact that eating Cheetos turns their fingers orange with residual cheese dust. In her background note, Karmarkar cites an article in the August 2011 issue of *Fast Company,* which describes how the EEG patterns indicated "a sense of giddy subversion that consumers enjoy over the messiness of the product."

Ethical Issues Associated with Neuromarketing

Since the field of neuromarketing is gaining momentum and attention, it has also experienced resistance from those who oppose this type of research based on ethical reasons. Among the most vocal of these opponents is the nonprofit consumer protection group Commercial Alert. This agency is raising awareness about the ethical implications of neuromarketing, namely: Is it ethical to conduct such research and development, since these techniques and activities could open the door to unprecedented and possibly abusive influence over consumers? The following five questions raise additional ethical concerns about neuromarketing.

Ethical Question 1: Does the practice of "reading people's minds"—or at least observing brain scans to get clues on how consumers react to targeted buying practices and objects—give marketers an unfair and potentially harmful advantage over consumers?

Neuromarketing practices could potentially give corporations an unfair advantage over consumers' choices and buying activities. Because marketers could gain access to a consumer's inner thoughts and opinions, some of which the consumer may not even be aware, this power could easily be misused. According to a *Fast Company* article by Kevin Randall, "consumer advocates and other groups have claimed neuromarketers are exploiting people to 'sell us crap we don't need' and creating unhealthy and irresponsible addictions and cravings." Advocacy group Commercial Alert agreed. In a letter sent to Senate Commerce Committee chairman John McCain in 2004, the group quoted Adam Koval, a neuromarketing pioneer, stating that this new technology "will actually result in higher product sales or in getting customers to behave the way [corporations] want them to behave." These arguments raise an ethical question with regard to whether a company should have this type and amount of power over consumers' buying behavior.

Ethical Question 2: What if neuromarketing is used by politicians or groups with extreme political interests?

Consider the effects of a political party utilizing neuromarketing to influence voter decisions. If these groups have the power to learn from their constituents' thoughts and opinions, they could also have an enormous advantage in persuading them to vote a certain way in elections. Some advocacy groups fear that this power will be abused by politicians. In the letter sent to Senator McCain by the advocacy Commercial Alert, the group noted that "political consultants have already teamed up with neuroscientists . . . to conduct neuromarketing

experiments to gauge the effectiveness of political advertising." The power of neuromarketing could also potentially be exploited by extreme political or social groups to engage in dangerously effective propaganda campaigns. What if extremist regimes had had this technology? Could they have been even more powerful in their anti-Semitic campaign and perhaps faced less resistance from enemies around the world? Writers in *Fast Company* and Commercial Alert even go so far as to suggest that neuromarketing could be used by some politicians or extremist groups to "brainwash" the public into accepting their political or social viewpoints.

Ethical Question 3: When does knowing an individual's subconscious thoughts cross the line of privacy invasion?

Since the September 11 attacks and subsequent Patriot Act legislation, privacy has been a hot topic. The introduction of neuromarketing aggravates issues of individual privacy. It was questioned whether recording a person's telephone conversations or tracking Internet activity was an invasion of privacy, and gaining access to an individual's subconscious thoughts is far more serious. Some marketers argue that this technology is advantageous in that it can reveal a consumer's inner feelings or motivations that cannot be obtained through a focus group, either because the person is unaware of them or because he or she lies about them. But shouldn't the consumer have the right to disclose only the information that they are conscious of and deem acceptable to share with a corporation? Circumventing the individual's judgment on these matters through the use of neuromarketing could be considered an unfair violation of privacy.

Ethical Question 4: Could increases in marketing effectiveness lead to higher levels of "marketing-related diseases" that are already having harmful effects on American society?

Consumer advocacy groups have long argued that corporations use marketing to promote so-called marketing-related diseases, including obesity, diabetes, smoking-related illnesses, alcoholism, and eating disorders, such as anorexia and bulimia. Consumer advocates feel that some marketers and marketing practices that glorify ultrathin models or excessive alcohol consumption play a major role in perpetuating these diseases in the American society. With the effectiveness that could be added to these types of advertisements through the use of neuromarketing, some fear that these illnesses will become even more pervasive, especially among young people who are traditionally more susceptible to marketing messages. According to Commercial Alert's letter to Senator McCain, "The use of neuromarketing by companies that produce tobacco, alcohol, junk food, or fast food could be damaging to public health. For example, what if Neuromarketing helped tobacco companies to increase the effectiveness of their marketing by a mere 2%? Smoking causes 440,000 premature deaths in the United States annually. A back of the hand calculation suggests that this could eventually cause approximately an extra nearly 9,000 premature deaths per year."

Ethical Question 5: Related to the above issue, could neuromarketing be used to irresponsibly target young consumers?

Some marketing practices often and more easily influence the youth in a society. Children and teenagers are known to be the easiest segments to target and persuade through mass-media advertising and other marketing tactics. Consumer protection groups have been formed to fight against corporations that are believed to be unethically targeting children, particularly during children's television programming. Commercial Alert has been a major player in this area, stating that "Corporations regularly promote . . . to children and teenagers degraded values and products including materialism, addiction, violence, gambling, pornography, anti-social behavior, etc. Any increase in the effectiveness in the marketing of these values and products could impact the character of millions of Americans." With neuromarketing technology, these organizations will have greater power to influence levels of demand among already susceptible groups of consumers.

The Stakeholders

The focal stakeholders in this case are the neuromarketing companies, such as NeuroFocus, EmSense, and Sands Research. Other stakeholders include: experts in both marketing and neuroscience that invest in neuromarketing companies; experts against neuromarketing; brands that utilize neuromarketing in their strategy; brands that do not utilize neuromarketing; neuromarketing competitors (i.e., traditional marketing agencies); consumers; Commercial Alert and other consumer rights groups; political groups; the media; lawyers; and legislatures.

Neuromarketing companies are forming coalitions with marketing and neuroscience experts. Gaining the support of experts supports the argument that neuromarketing is an ethical, efficient, and effective practice. Neuromarketing companies are also forming coalitions with companies such as Frito-Lay, Pepsi-Cola, Microsoft, and Hyundai. However, experts and consumers who are not in agreement with the use of neuromarketing are forming their own coalitions to improve awareness of the ethical implications of neuromarketing. The *New York Times* and *Fast Company*, as noted earlier, have started covering the issue in recent years. Blogs such as Robert Dooley's "Neuromarketing: Where Brain Science and Marketing Meet" (http://www.neurosciencemarketing.com/blog/) have cropped up to discuss questionable issues about neuromarketing. PBS has also run programming and hosted discussions on the issue on its web site.

Whether or not and to what extent neuromarketing practices are used in ethically questionable ways remains a topic of debate. Mapping the stakeholders and their different interests and strategies will help clarify who may be getting hurt and who may also benefit.

Questions for Discussion

1. Do you believe that neuromarketing is unethical or an innovative business practice? Explain.
2. Do all or most companies that market products and services use questionable techniques to influence and persuade customers?

3. Are you personally concerned or bothered by the neuromarketing techniques described in this case? Explain.
4. What moral responsibilities, if any, should marketing companies have—especially those firms using neuromarketing techniques? Explain.

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Case 15

Wal-Mart: Challenges with Gender Discrimination

The Civil Rights Act of 1964 forbids gender-based discrimination in the employment arena. Section 703 of this act specifies that:

> It shall be an unlawful employment practice for an employer to fail or refuse to hire or to discharge any individual, or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual's race, color, religion, sex, or national origin.
>
> It shall be an unlawful employment practice for an employer to limit, segregate, or classify his employees in any way which would deprive or tend to deprive any individual of employment opportunities or otherwise adversely affect his status as an employee, because of such individual's race, color, religion, sex, or national origin.

In *Dukes v. Wal-Mart Stores, Inc.,* Betty Dukes, the lead plaintiff along with five other plaintiffs and the class that they represent, charged that "Wal-Mart discriminates against its female employees by advancing male employees more quickly than female employees, by denying female employees equal job assignments, promotions, training and compensation, and by retaliating against those who oppose its unlawful practices." In addition, the plaintiffs sought to end Wal-Mart's discriminatory practices, to receive relief for the class, and to secure punitive damages. *Dukes v. Wal-Mart Stores, Inc.* also alleged that Wal-Mart's underlying culture and policies contributed to the discrimination that the plaintiffs experienced.

"The theories pursued in the Dukes litigation involve what are known as 'glass ceiling/sticky floor' allegations of employment discrimination that female employees are relegated to low-paying positions and are unable to be promoted into better paying and higher-level managerial jobs." Note that "These arguments manifest an aggressive approach by the plaintiffs' bar to establish the class-worthiness of claims stretching over multiple facilities with assertions that pay and promotion claims are readily susceptible to class-action treatment based on expert testimony that such claims are truly common and typical." According to data supplied by statistical consultant Richard Drogin on behalf of the plaintiffs, Wal-Mart had an established pattern of discrimination against women. In his statistical report, Drogin concluded that "Women employees at Wal-Mart are concentrated in the lower paying jobs, are paid less than men in the same job, and are less likely to advance to management positions than men. These gender patterns persist even though women have more seniority, have lower turnover rates, and have higher performance ratings in most jobs. The shortfall in female earnings, pay rates, and promotion rates has a high degree of statistical significance."

Wal-Mart's expert witness, Joan Haworth, an economist who had provided testimony in more than five dozen employment cases, reached different conclusions

regarding pay disparity at the giant retailer. She claimed that "Drogin's analyses did not adequately take into account crucial factors, like the number of hours worked and whether they included night-shift work, which pays more. But her overarching criticism was that his approach amounted to pretending that a single person was making all promotion and pay decisions throughout Wal-Mart nationwide, when, according to depositions, most pay determinations were made at the store manager level or, in the case of certain specialty department employees, at the district manager level." She concluded that "more than 90% of class members worked at stores where women were statistically no worse off than men. Wal-Mart's argument, then, was that if a class action must be filed, it should be brought against the specific stores with disparities favoring men."

Class Action or Not?

Perhaps the most contentious issue in the *Dukes v. Wal-Mart Stores, Inc.* case has been whether or not a class action is warranted. A class-action filing is affected by Rule 23 of the Federal Rules of Civil Procedure, which prescribes the conditions under which class-action suits may be brought to Federal courts. Rule 23(a) outlines the prerequisites for a class action. They are: "(1) the class is so numerous that joinder of all members is impracticable; (2) there are questions of law or fact common to the class; (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class; and (4) the representative parties will fairly and adequately protect the interests of the class."

Wal-Mart challenged the legal validity of a class action in the case, arguing, in a September 24, 2003 hearing before U.S. District Judge Martin Jenkins, that the lawsuit should be broken into separate class actions against each of the 3,473 stores across the United States because decisions about pay and promotions are largely made at the store level. On June 22, 2004, Judge Jenkins ruled that six current and former Wal-Mart employees from California may represent all female employees of Wal-Mart who worked at its U.S. stores anytime since December 26, 1998. In his findings, Judge Jenkins said that the evidence presented by the plaintiffs "raises an inference that Wal-Mart engages in discriminatory practices in compensation and promotion that affect all plaintiffs in a common manner."

Judge Jenkins' ruling is potentially momentous because "Class-action litigation is unlike a single plaintiff lawsuit in that the stakes are enormous and the exposure to a corporation increases geometrically if the plaintiffs are successful. The holy grail of class-action litigation for both sides is the class certification decision. . . . Practically speaking, victory or defeat in the class certification process casts the die for a corporation's exit strategy from class-action litigation."

Enter the United States Court of Appeals for the Ninth Circuit

On appeal to the Ninth Circuit, located in San Francisco, California, Wal-Mart claimed that the proposed class failed to meet the commonality prerequisite of Rule 23(a)(2), since local store managers had autonomy in making salary and promotion decisions. However, "the plaintiffs said this hands-off approach itself

constituted the common policy that impacted class members—arguing it fostered discrimination by allowing individual managers to make excessively subjective decisions based on gender stereotypes." In support of this position, plaintiffs presented evidence from an expert witness, sociologist William Bielby, who based his testimony on so-called "social framework analysis." Bielby testified that "a strong and widely shared organizational culture promotes uniformity of practices throughout an organization," and that such a culture "could be inferred from such factors as Wal-Mart's emphasis on the company's founder and its history, a mission statement defined by core values, [and] frequent communication about the culture to employees." Allan King, an interested observer who has a doctorate in labor economics and a law degree, says, "There is no such thing as social framework analysis. . . . But it will be a challenge for defendants to persuade the court that what they [i.e., plaintiffs' expert witnesses] regard as a methodology is not." Ultimately, the Ninth Circuit used Bielby's testimony to support its finding that commonality had been demonstrated for the class. The court wrote, "Evidence of Wal-Mart's subjective decision-making policy raises an inference of discrimination and provides further evidence of a common practice."

On February 6, 2007, the United States Court of Appeals for the Ninth Circuit affirmed, on a 2–1 vote, U.S. District Court Judge Martin Jenkins' decision to certify a class that had grown to approximately 2 million women in the lawsuit against Wal-Mart. The class includes the more than 2 million women who have worked at any of the company's more than 4,000 retail stores nationwide since December 26, 1998. Writing for the majority, Judge Harry Pregerson "deferred to the district court's 'broad discretion' to certify and did not amend any of its findings." Most of the Ninth Circuit Court's opinion addressed the commonality prerequisite of Rule 23(a)(2). The Ninth Circuit's opinion said that "Plaintiffs demonstrated that Wal-Mart had a corporate policy of discrimination (because the policy was corporate-wide, it would be in effect at every Wal-Mart store and thus would be common to every female Wal-Mart employee)." However, in a strongly worded dissent, Judge Andrew J. Kleinfeld said the appellate decision "poses a considerable risk of enriching undeserving class members and counsel, but depriving thousands of women actually injured by sex discrimination their just due."

In response to the Ninth Circuit's ruling, Theodore J. Boutrous Jr., an attorney representing Wal-Mart, said, "We recognize this is another step in what is going to be a long process. It's a technical legal ruling that only certifies the lawsuit as a class action, but does not address its merits." Boutrous also expressed the belief that Wal-Mart has a strong argument for obtaining further review from either the full Ninth Circuit Court or the United States Supreme Court, "because the majority rule conflicts with many Supreme Court decisions as well as many recent decisions from other appellate courts around the country that 'have rejected precisely the direction taken by the [Ninth Circuit] court.'" However, Brad Seligman, representing the Wal-Mart plaintiffs, said the appellate court was now the second court to rule on the class certification issue and "it's clear Wal-Mart

is going to have to face the music and justify its practices, and we are very optimistic this case will ultimately be returned to trial." In fact, Wal-Mart asked the full Court of Appeals for the Ninth Circuit to reconsider the 2–1 approval of the class.

In May 2011, the Supreme Court started hearing the *Dukes v. Wal-Mart Stores, Inc.* case. In June, "the Court ruled that the case could not proceed because the 1.5 million current and former Wal-Mart employees suing the company for alleged sex discrimination could not legally constitute a 'class.'" Therefore, Wal-Mart successfully defended its position, and from then on the criteria for getting a class-action suit approved has been much stricter.

Potential Implications of *Dukes v. Wal-Mart Stores, Inc.*

Observers say the 2–1 decision by the Ninth Circuit Court of Appeals does not break any new legal ground even though it could end up costing Wal-Mart billions of dollars. Rather, the primary significance of the ruling is the unprecedented size of the class action. Anthony J. Oncidi, an attorney with Proskauer Rose LLP in Los Angeles, said Judge Kleinfeld's strong dissent in the 2–1 ruling suggests that other Ninth Circuit judges may also believe that the 2–1 majority ruling is not really appropriate, which could lead to a reexamination by the full appellate court. Ultimately, the Supreme Court "may respond to business community demands that it 'tighten up class certification' in the same way it tightened rules on punitive damages."

Although *Dukes v. Wal-Mart, Inc.* may not break any new legal ground, employers nonetheless may want to rethink their practices. As Susie Gibbons, an attorney with Poyner & Spruill L.L.P. in Raleigh, North Carolina, says, "The huge potential liability of this case represents an expansion of the class action vehicle as a weapon of attack against employers, and it should cause all companies of any size to review their own hiring and promotional practices. . . . If I were a risk manager at a company, I would want to analyze this case to look at what the vulnerabilities were that ended up causing this problem for Wal-Mart." Writing in *Fortune* magazine, Roger Parloff and Susan Kaufman point out that although racial or gender quotas and preferences are illegal, "they will obviously be tempting to employers who want to avoid being hit with class-action employment discrimination lawsuits. For there is only one sure-fire way to inoculate oneself against such suits, and that is to have workforce numbers that look good even when analyzed by a plaintiffs' expert. And the cheapest and fastest way to get those is to use quotas or preferences."

Mary Swanton, writing in *InsideCounsel,* says that "employers can use the findings in Dukes to assess their vulnerabilities. For example, companies could test how their corporate culture would stand up to a sociologist's analysis. They also could look at how their decision-making processes can be made more objective and whether they have processes in place to ensure their managers implement non-discrimination policies." Meg Campbell, with Ogletree, Deakins, Nash, Smoak & Stewart, says, "If they [employers] take the lesson of this court's analysis and look at what they are doing and how they can do it better, they'll put themselves in the best defensive posture in the event of litigation."

Parloff and Kaufman also remark, "The Wal-Mart rulings could end up representing a high-water mark. . . . The underlying legal battles seem destined for the [United States] Supreme Court. The urgent question is whether the current [Supreme] Court with its staunchly conservative five-justice majority, sharp aversion to race-conscious remedies, and weak respect for prior precedent will allow this situation to persist. The Wal-Mart suit may be the case that gives us the answer."

Questions for Discussion

1. Based on the stated human resources philosophy of Wal-Mart, would it be likely that the company would discriminate based on gender differences? Explain.
2. Put yourself in the role of the plaintiffs. What ethical arguments would you offer in support of their allegations?
3. Put yourself in the role of Wal-Mart. What ethical arguments would you offer to counter the plaintiffs' allegations?
4. What do you think the plaintiffs meant by their allegation that Wal-Mart's culture is a significant contributor to gender discrimination?
5. Is a class action against Wal-Mart justified? Explain your position.
6. Explain how the outcome of *Dukes v. Wal-Mart Stores, Inc.* is important for major stakeholders in the case, including the American society.

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Wal-Mart's corporate web site asserts that: "Wal-Mart will not tolerate discrimination in employment on the basis of race, color, age, sex, sexual orientation, religion, disability, ethnicity, national origin, veteran status, marital status or any other legally-protected status." Against this backdrop of professed commitment to equal opportunity, Wal-Mart faces an ongoing battle in the gender discrimination class action suit Dukes v. Wal-Mart Stores, Inc. filed on June 19, 2001 in United States District Court for the Northern District of California.

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Case 16

Vioxx, Dodge Ball: Did Merck Try to Avoid the Truth?

Overview

On September 30, 2004, Merck & Company ("Merck") voluntarily withdrew Vioxx (rofecoxib), its blockbuster arthritis drug that had been on the market since 1999. Since 2001, Merck had been facing accusations that Vioxx increased the risk of heart attack and stroke for those patients taking the drug for longer than 18 months. In a press release announcing the voluntary, worldwide withdrawal, Merck executives felt that although Merck could continue marketing the drug with new labels that incorporated the results of recent trials, the responsible action was to remove the product from the market. Since the withdrawal, thousands of lawsuits have been brought against Merck, and several questions remain, most notably: Did Merck suppress data early on, and will Merck be able to withstand the thousands of lawsuits that will take place in the coming years?

The Beginning

Millions of Americans suffer from arthritis pains, with levels of pain that vary from minor to severe. Arthritis is a general term that means "joint inflammation," and there are more than 100 different types of rheumatic conditions and diseases that can cause joint inflammation. Different types of non-steroidal anti-inflammatory drugs ("NSAIDs") can be taken, ranging from ibuprofen to naproxen. The Cox-2 inhibitors were new drugs that were developed to block the Cox-2 enzyme, which is responsible for sending chemicals within the body that cause pain and inflammation. Merck and Pfizer, two of the largest pharmaceutical companies in the world, burst onto the scene in 1999 with their Cox-2 inhibiting drugs, Vioxx and Celebrex. Buoyed by the emerging trend of direct-to-consumer ("DTC") marketing, these companies began a marketing blitz targeting the general public.

In 2001, the National Institute for Health Care Management Research and Educational Foundation released a report on the growing DTC trend. The report showed that in 2000, Merck spent $160 million to advertise Vioxx, as compared to PepsiCo's $125 million to advertise Pepsi, Budweiser's $146 million to advertise its beer, and Pfizer's $78 million to advertise Celebrex. This caused Merck's sales of Vioxx to increase 360% from 1999 to 2000, while Pfizer's sales of Celebrex increased 58% in that same period. Before the drug was approved, Merck had followed industry standard testing procedures. In 1998 however, an internal trial, study "090," revealed a higher number of cardiovascular problems in patients taking the drug, compared to those not taking Vioxx. The study showed that patients taking Vioxx were six times more likely to have a cardiovascular event than those taking a different arthritis drug or placebo. Merck felt that this test was too small (978 patients), and not statistically significant. Merck received approval from the FDA in 1999 to begin selling the drug, just behind Pfizer's release of Celebrex.

Merck's Studies

In 1999, Merck launched another study on Vioxx, entitled VIGOR. The VIGOR study was the Vioxx Gastrointestinal Outcomes Research Study, and included 8,000 patients. The purpose of this study was to determine if Vioxx was any less damaging on the stomach than naproxen. NSAIDs, such as naproxen, have side effects that often include gastrointestinal problems and can cause abdominal pain, heartburn, and/or diarrhea. Of the 33 million Americans taking NSAIDs, between 10 and 50% develop these side effects; many so severely that they must stop taking NSAIDs due to stomach ulcerations. The Cox-1 enzyme produces mucus that protects the stomach lining, and many NSAIDs, such as naproxen, block both the Cox-1 and the Cox-2 enzymes. The benefit of these new Cox-2 inhibiting drugs was that the Cox-1 enzyme was not blocked, and could thus continue to protect the stomach lining.

The results of this test proved that Vioxx did produce significantly less upper gastrointestinal events than naproxen. However, the tests revealed additional information: Patients taking Vioxx for more than 18 months were five times more likely to suffer a heart attack than those who took naproxen. At the time, Merck executives stated that this finding was due to naproxen's ability to protect the heart, not due to any specific issue with Vioxx. These results were published in the *New England Journal of Medicine* in 2000. At that time, many industry experts began to doubt the safety of Vioxx based on the results of the VIGOR study and the "090" study. Despite the results of these studies, Merck continued its advertising in 2000 and 2001. Between 1999 and 2003, Merck generated approximately $2.3 billion in sales. In 2001, the FDA recommended that Merck include warnings on Vioxx labels, and also took issue with a misleading promotional campaign.

In a letter to Raymond Gilmartin, the president and CEO of Merck, Thomas Abrams, a director in the division of drug marketing, advertising, and communications, warned Merck that it had made false statements, used unsubstantiated claims, omitted risk information, and used audio conferences to promote Vioxx for unapproved usages and unapproved dosage. Note that "Abrams has been on all sides of drug marketing, from receiving promotions as a pharmacist to creating promotions as a member of industry to regulating promotions as the head of DDMAC. As such, he's in good position to see the big picture." The following is an excerpt from the letter:

> You have engaged in a promotional campaign for Vioxx that minimizes the potentially serious cardiovascular findings that were observed in the Vioxx Gastrointestinal Outcomes Research (VIGOR) study, and thus, misrepresents the safety profile for Vioxx. Specifically, your promotional campaign discounts the fact that in the VIGOR study, patients on Vioxx were observed to have a four- to five-fold increase in myocardial infarctions (MIs) compared to patients on the comparator non-steroidal anti-inflammatory drug (NSAID), Naprosyn (naproxen).

In 2002, Merck added language to the Vioxx label that disclosed the cardiovascular risks that were associated with Vioxx. Despite these warnings and the

studies, Vioxx accounted for $2.5 billion in sales in 2003 alone, with more than 91 million Vioxx prescriptions written throughout the history of the drug.

In 2000, Merck began a different study, this time to determine if Vioxx could successfully prevent the recurrence of colon polyps. This study was called APPROVe: the Adenomatous Polyp Prevention on Vioxx trial. The results of this trial echoed the results of the prior trials. Of the more than 2,600 patients that took part in the trial, those patients taking Vioxx for more than 18 months found themselves at a higher risk for cardiovascular events than those on a placebo. Specifically, the Vioxx patients were twice as likely to suffer an event as those not taking Vioxx. It was with this information that Merck decided to pull the drug in 2004.

Dodge Ball and Vioxx

While Merck was busy conducting internal studies, the sales force was being trained to handle the increasing amount of questions regarding the risks of cardiovascular events. When salespersons called on physicians, the questions of the risks were more frequent, such as, "I am concerned about the cardiovascular effects of Vioxx" and "I use Celebrex. I'm concerned with the safety profile with Vioxx." The name of this document was "Dodge Ball Vioxx." The 46-page document described the activities used to train the sales force, and included Jeopardy!-like question-and-answer sections to help the Vioxx reps learn how to correctly answer or deflect physicians' questions. A 12-page list of categories was presented to the sales force, but many representatives were very concerned with the process. In a 2004 interview with 60 Minutes, a rep who did not wish to be named said, "We were supposed to tell the physician that Vioxx did not cause cardiovascular events; that instead, in the studies, Naproxen has aspirin-like characteristics which made Naproxen a heart-protecting type of drug where Vioxx did not have that heart-protecting side." The rep added, "I put my reputation on the line. I gave my physicians my word that Vioxx was a safe, effective product and it's been pulled from the market because it was killing people."

The final page of this 46-page training document highlighted the five top messages for Vioxx in 2000, and, in the last paragraph, stated, "This document must not be copied, distributed, or shown to anyone outside the company." This training document was one of the areas the FDA commented on when it notified Merck that it was engaging in promotional campaigns attempting to minimize the risks associated with Vioxx.

Outside Opinions and Studies

When the internal Merck studies, "090" and VIGOR, were released, many in the medical community were concerned with the results, especially considering that Vioxx was a potential blockbuster drug that could be used by more than one hundred million worldwide. One such critic was Dr. Eric Topol, who was the chief of cardiovascular medicine at the Cleveland Clinic. Topol first began questioning the studies and Merck's responses in 2001. On October 21, 2004, Topol published an article in the *New England Journal of Medicine*, in which he outlined

the case against Merck and the FDA. As he recounted the results of the "090," VIGOR, and APPROVe studies, he noted that "Only by happenstance, in a trial involving 2600 patients with colon polyps who could not have been enrolled if they had had any cardiovascular disease" was it discovered that there was an increased risk of cardiovascular events. Topol felt that neither Merck, nor the FDA, had fulfilled their responsibilities to the public based on the risks that were seen in the earlier studies. His own research of Cox-2 inhibitors and other medicines available showed a "very substantial worrying risk of heart attacks and strokes." He added, "So if you have Study '090,' and you want to discount that somehow, then you have VIGOR. You've got two trials now. You have essentially lightning striking twice. That's independent replication. That's really serious confirmation. This is unequivocal. This is a problem." Merck researchers responded to Dr. Topol's "Perspective" article with their own "Correspondence." In this correspondence, the researchers stated that Topol's timeline was false, and that other studies conducted by Merck did not show any increased risks in cardiovascular events versus placebo.

A common trend in the industry is that doctors consult for financial firms. A December 2004 edition of *Fortune* magazine identified a potential conflict of interest for Topol. He was on the scientific advisory board of a hedge fund, the Biomedical Value Fund, run by Great Point Partners. This fund, with more than $170 million in assets, performed very well in 2004, and much of this was due to the firms "shorting" of Merck. Selling "short" is a term used to describe when an investor is looking to profit from a stock's falling price. In a performance summary published in September 2004, Great Point Partners singled out Topol for his contribution to the increased earnings. "Vioxx, while good for your arthritis, can be very bad for your heart. Eric Topol, M.D., of our Medical Advisory Board, has been singing this tune since 2002, and we were on the right side [short] of that situation." When *Fortune* confronted Topol with this information, he immediately resigned from the board. Since this time, Merck lawyers have introduced this information to build the case that Topol has a personal "vendetta" against Merck. In late 2005, Topol was demoted at the Cleveland Clinic. In February 2006, Topol announced that he would be leaving the clinic to teach at a nearby medical school.

The Recall and Initial Lawsuits

On September 30, 2004, Merck voluntarily withdrew Vioxx from the market after the results of the APPROVe trial. Merck had made it clear that this was a voluntary recall, and that it was due to the heightened risk of cardiovascular events. Merck's CEO and president, Raymond Gilmartin, maintained that Merck could have relabeled the packaging to include warnings about the cardiovascular risks, but concluded that the voluntary withdrawal was the "responsible" action to take. But the already skeptical medical community was aware of the "090" and VIGOR studies. One month later, a study conducted by the FDA using information from approximately 1.4 million patients in the Kaiser Permanente

health care organization found that the use of Vioxx more than tripled the patient's risk of a cardiovascular event. Based on the number of Vioxx prescriptions written between 1999 and 2003, the study estimated that Vioxx may have contributed to more than 27,785 heart attacks or sudden cardiac arrests. This was initially published by the *Wall Street Journal*, but the results were never published by the FDA.

After the recall, word of the studies and their results began reaching the public. The legal system became flooded with activity. On August 19, 2005, the first lawsuit against Merck reached its conclusion in a Texas courtroom. Carol Ernst sued Merck, claiming that her husband Robert died in 2001 of an irregular heartbeat caused by Vioxx. Ernst's lawyer argued that Merck continued with an aggressive marketing campaign for Vioxx, even though it was aware of the increased risk of a cardiovascular event for patients taking Vioxx. The jury agreed with Ernst, and awarded $229 million in punitive damages and $24.4 million in compensatory damages. Texas law sets a cap on punitive damages, however, and analysts believe that they may be reduced to $1.6 million. Merck maintains that they will fight the results of this decision.

As of January 31, 2006, Merck faced 9,650 Vioxx-related lawsuits. In 2004, Merck set aside $675 million to use for legal fees in defending itself in the Vioxx lawsuits. In 2005, Merck used $285 million, and was forced to replenish this reserve with another $295 million, bringing the total to $685 million for legal fees alone. Merck has yet to pay any damages, including the $253 million awarded to Carol Ernst in 2005. However, Merck is prepared to fight each lawsuit separately and not push for a class-action lawsuit. In the three lawsuits previously filed against the company, Merck lost one case, won one case, and had a mistrial declared in the third. Jury selection for a retrial of the mistrial began on February 6, 2006, and a fourth case was underway in Texas for the heart attack death of a 71-year-old man.

Vioxx and Merck: Update

Merck's official web site announces that "The meeting of the thresholds with enrollment documents in compliance with the Settlement Agreement would obligate Merck to pay $4.85 billion in installments into the resolution fund. In 2007, the Company recorded a pretax charge of $4.85 billion, which represents the fixed amount to be paid by the Company to settle qualifying claims.

The thresholds are: (a) 85% or more of all eligible MI claims; (b) 85% or more of all eligible IS claims; (c) 85% or more of all eligible claims claiming death as an injury; and (d) 85% or more of all eligible claims alleging more than 12 months of use."

As of March 31, 2008, the claims administrator reports more than 28,250 eligible MI claimants have initiated enrollment and more than 16,750 eligible IS claimants have initiated enrollment. Of these, more than 5,500 eligible MI and IS claimants alleging death as an injury have initiated enrollment, and more than 27,500 eligible MI and IS claimants alleging more than 12 months of use have

initiated enrollment. Each of these numbers appears to represent at least 94.5% of the eligible claims in each category. These numbers do not include an additional 5,500 enrollees whose eligibility has yet to be determined.

On Thursday [July 17, 2008] more than 97% of eligible U.S. claimants had elected to participate in its $4.85 billion proposed Vioxx settlement, an adequate number to trigger funding of the program."

"The company expects that the distribution of interim payments to qualified claimants will begin in August and will continue on a rolling basis until all claimants who qualify for an interim payment are paid," Merck said in a news release. A Merck spokesperson said on July 17, 2008 that over 48,500 of approximately 50,000 people registered as eligible injuries had enrolled in the program.

With the increase scrutiny on corporate social responsibility, and the serious consequences that can arise if a pharmaceutical company is accused of violating public trust, companies such as Merck have been doing business on a slippery slope. Industry analysts reported after Vioxx's settlement that "the FDA has become far more careful about approving new medicines in the wake of the Vioxx withdrawal and criticism of the agency's oversight of the medicine."

Pharmaceutical companies have created many lifesaving drugs over the years, and have helped hundreds of millions of people. However, if a company is perceived to act unethically and violates the public trust, that company stands to face not only more lawsuits, but the loss of customers and the financial resources that help these companies succeed. Will this settlement be the last for Merck? Or, is this just another cost of doing business for the pharmaceutical giant operating in a highly profitable and uncertain industry sector?

Aftermath

Merck in 2011 also paid an additional $950 million in a later settlement that completed Merck's marketing practices by the government. In yet another 2013 settlement, customers claiming to have been "duped" into purchasing Vioxx were reimbursed $23 million. Vioxx has cost Merck over $5.8 billion. "The settlement of a seven-year U.S. government investigation brings Merck closer to resolving the mountain of litigation that followed the company's 2004 withdrawal of the big-selling drug from the market after a study showed it increased the risk for heart attacks and strokes. It marks the latest big payout by a drug company to settle health-care fraud allegations, underscoring heightened government scrutiny of the way drug makers do business."

Questions for Discussion

1. What were the first warning signals that Vioxx may have been unsafe for patients?
2. Who was responsible in this case for stopping the harm that occurred from the Vioxx drug, and at what point could the harm have been prevented? Explain.

3. Summarize Dr. Topol's ethics as demonstrated in this case. What were his motives here?
4. What role did the sales force representatives play in this case?
5. Who ultimately is to blame in this case for the harm caused by Vioxx?
6. Should Merck be singled out as a major culprit in this case or is this "business as usual" for pharmaceutical companies?

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6

THE CORPORATION AND INTERNAL STAKEHOLDERS

Values-Based Moral Leadership, Culture, Strategy, and Self-Regulation

6.1 Leadership and Stakeholder Management

Ethical Insight 6.1

Ethical Insight 6.2

6.2 Organizational Culture, Compliance, and Stakeholder Management

6.3 Leading and Managing Strategy and Structure

6.4 Leading Internal Stakeholder Values in the Organization

6.5 Corporate Self-Regulation and Ethics Programs: Challenges and Issues

Ethical Insight 6.3

Chapter Summary

Questions

Exercises

Real-Time Ethical Dilemmas

Cases

17. Kaiser Permanente: A Crisis of Communication, Values, and Systems Failure
18. Social Networking and Social Responsibility

Notes

OPENING CASE

Two Leaders' Ethical Styles

Warren Buffet, Berkshire Hathaway

Founder and chief executive officer (CEO) of Berkshire Hathaway, Warren Buffett has taken unprecedented steps in recent years to ensure that his messages about investing, ethics, and philanthropy reach an audience that will survive him. He didn't invent the light bulb, but he's had lots of bright ideas. He didn't devise the mass-production assembly line, but his companies have sold masses of goods. And Warren Buffett didn't originate the concept of money, but he has more of it than most–he has been listed as the second most wealthy business person

by *Forbes* for several years. So what will be the Omaha investor's legacy? Or, rather, his legacies? Observers say the 83-year-old's ideas and philosophy of business and life will last far beyond his own. "Somebody from this group will learn something that will affect their lives," Buffett told a group of graduate students during a 2005 visit to Omaha.

"Buffett's emphasis on working with ethical people is already influencing business leaders and business schools, a change that could last far into the future," said Bruce Avolio, director of the University of Nebraska-Lincoln's Leadership Institute. "He buys the culture when he invests in an organization," Avolio said, "valuing a business's human condition as much as its financial condition. That's shifting people's thinking, and it has a huge impact. It's a model that's replicable–treating people fairly. Integrity underlies not only Warren Buffett's investments but also his philosophy of life." Keith Darcy, head of the 1,400-member Ethics and Compliance Officers Association in Waltham, Massachusetts, said Buffett has played a hand in "a flight to integrity" by investors, executives, employees, suppliers, and customers, who want to be involved with companies that do business correctly. "It's essential to him to be working with people he trusts," Darcy said. "Without that level of trust, it's not worth doing business. Certainly he has been an exemplar for understanding that when you make investments, character and reputation are everything." In meetings with students, Darcy said, Buffett "speaks from his heart. He certainly is a mythological figure, except he's not a myth, he's real–a man of enormous success who always has believed in investing in companies with inherent value, but in particular the people in those businesses." Darcy believes Buffett will be a role model far into the future. Buffett himself has stated: "I want employees to ask themselves whether they are willing to have any contemplated act appear on the front page of their local paper the next day, to be read by their spouses, children, and friends. . . . If they follow this test, they need not fear my other message to them: Lose money for the firm, and I will be understanding; lose a shred of reputation for the firm, and I will be ruthless."[1]

Ratan Tata, Former Chairman of the Indian Corporation Tata Group

Ratan Tata retired on his 75th birthday after leading the Indian corporate conglomerate, the Tata Group. He assumed leadership from his uncle in 1991. The so-called House of Tata owns over 100 companies in 80 countries, including the Taj Group of luxury hotels and the exclusive Tata Nano car. The group's holdings exceed those of Wal-mart or ExxonMobil. The Tata Group was the first Indian company to obtain $100 billion in revenues, half of which is from abroad. Ratan Tata helped acquire significant European enterprises, including Jaguar Land Rover and Corus, the Anglo-Dutch steelmaker. Under his leadership, this group is now "perceived to represent Indian capitalism at its best,

enjoying the goodwill of millions of customers, the loyalty of more than 400,000 employees and the investments of 3.8 million shareholders, while also reinvesting a substantial part of its profits into philanthropic work overseen by a set of trusts."[2] His ethical beliefs are embodied in the company's policies, as stated in the company's Article and Rules for Sustaining CSR, Clause No. 10:

> A Tata Company shall be committed to be a good corporate citizen not only in compliance with all relevant laws and regulations but also by actively assisting in the improvement of the quality of life of the people in the communities in which it operates with the objective of making them self-reliant. Such social responsibility would comprise, to initiate and support community initiatives in the field of community health and family welfare, water management, vocational training, education and literacy and encourage application of modern scientific and managerial techniques and expertise. This will be reviewed periodically in consonance with national and regional priorities. The company would also not treat these activities as optional ones but would strive to incorporate them as integral part of its business plan. The company would also encourage volunteering amongst its employees and help them to work in the communities. Tata companies are encouraged to develop social accounting systems and to carry out social audit of their operations.[3]

6.1 Leadership and Stakeholder Management

Leadership is the ability to influence followers to achieve common goals through shared purposes.[4] Leaders, with the help of followers, are responsible for enacting an organization's vision, mission, and strategies, and for achieving goals in socially responsible ways.[5] Leaders also help define the culture and model the values of organizations that are essential for setting and modeling the legal and ethical tone and boundaries. Warren Buffett, founder and CEO of Berkshire Hathaway and Rajan Tata, former chairman of the Tata Group, are two exemplary leaders among many others, who embody the ethical leadership values, characteristics, and actions this chapter addresses.

The CEO or president, who sometimes is also the chair of the board of directors, is the highest-ranking leader in a company. However, in both for- and not-for-profit organizations, the CEO reports to and is advised by the board of directors, which also serves leadership and governance roles. Leadership is not only limited to a few individuals or teams at the top of organizations. Individuals throughout an organization exert leadership responsibilities and influence in their roles and relationships to direct and guide their organizations.

Leadership also requires active involvement with and alignment of internal and external stakeholder relationships. Business relationships involve transactions and decisions that require ethical choices and, many times, moral courage. Building new strategic partnerships, transformational restructuring and lay-

offs, consumer lawsuits, environmental crises, bold new "green" initiatives, and turning around corporate cultures damaged by the effects of harmful products are examples of situations that require leadership business and ethical decisions. Leaders are responsible for the economic success of their enterprises and for the rights of those served inside and outside their boundaries. Research on leadership demonstrates that moral values, courage, and credibility are essential leadership capabilities.[6] James Collins' five-year research project on "good to great" companies found that leaders who moved from "good to great" showed what he called "Level 5" leadership. These leaders "channel their ego needs away from themselves and into the larger goal of building a great company. It's not that Level 5 leaders have no ego or self-interest. Indeed, they are incredibly ambitious—*but their ambition is first and foremost for the institution, not themselves*" (emphasis added).[7] Collins also concluded that Level 5 leaders build "enduring greatness through a paradoxical blend of personal humility and professional will."[8]

This chapter focuses on the challenges that values-based leaders face while managing internal stakeholders, strategy, and culture in organizations. From a stakeholder management approach, an organization's leaders are responsible for initiating and sustaining an ethical, principled, and collaborative orientation toward those served by the firm.[9] Leaders model and enforce the values they wish their companies to embody with stakeholders.[10] One of an organization's most prized assets is its reputation, as noted earlier in the text. Reputations are built through productive and conscientious relationships with stockholders and stakeholders.[11]

A stakeholder, values-based leadership approach determines whether or not the organization and culture:

- Are integrated or fragmented.
- Tolerate or build relationships.
- Isolate the organization or create mutual benefits and opportunities.
- Develop and sustain short-term or long-term goals and relationships.
- Encourage idiosyncratic dependent implementation based on division, function, business structure, and personal interest and style or encourage coherent approaches, driven by enterprise, visions, missions, values, and strategies.[12]

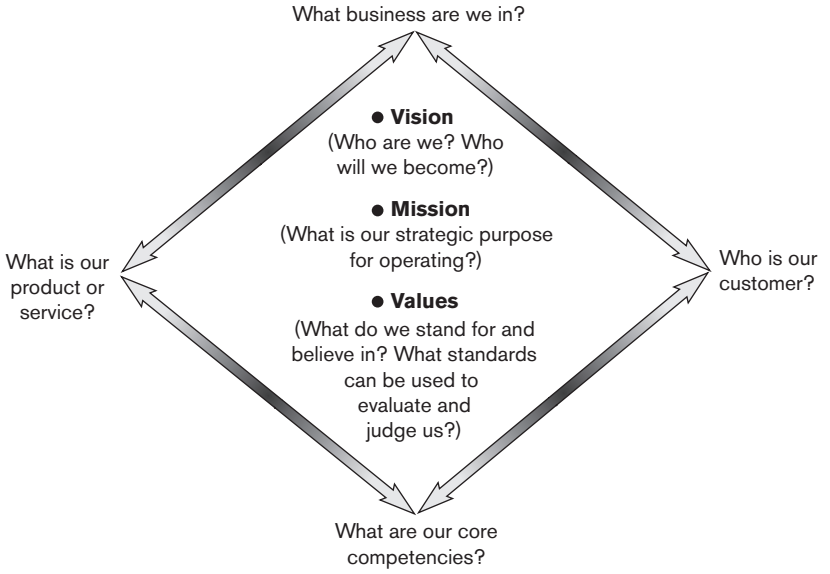
Effective leaders guide the ethical and strategic integration and alignment of the internal organization with the external environment. As the following sections show, competent leaders demonstrate different competencies in guiding and responding to their stakeholders and stockholders.

Defining Purpose, Mission, and Values

Leading an organization begins by identifying and enacting purpose and ethical values that are central to internal alignment, external market effectiveness, and responsibility toward stakeholders. As Figure 6.1 shows, key

Figure 6.1

Strategic Alignment Questions



Source: Joseph W. Weiss. © 2014.

questions executives must answer before identifying a strategy and leading their firm are centered on defining the organization's vision, mission, and values: *What business are we in? What is our product or service? Who are our customers? What are our core competencies?*

A values-based leadership approach is exemplified by Chester Barnard, who wrote in 1939 that effective leaders and managers "inspire cooperative personal decisions by creating faith in common understanding, faith in the probability of success, faith in the ultimate satisfaction of personal motives, and faith in the integrity of common purpose."[13] In the classic book *Built to Last,*[14] authors James Collins and Jerry Porras state, "Purpose is the set of fundamental reasons for a company's existence beyond just making money. Visionary companies get at purpose by asking questions similar to those posed by David Packard [cofounder of Hewlett-Packard]: 'I want to discuss why a company exists in the first place. . . . Why are we here? I think many people assume, wrongly, that a company exists simply to make money. While this is an important result of a company's existence, we have to go deeper and find the real reasons for our being.' "

JetBlue's founder and former CEO, David Neeleman, said:

> For our company's core values, we came up with five words: safety, caring, fun, integrity, and passion. We guide our company by them. But from my experience—and I've had a lot of life experiences that were deep religious

experiences—I feel that everyone is equal in the way they should be treated and the way they should be respected. I think that I try to conduct myself in that way. I treat everyone the same: I don't give anyone more deference because of their position or their status. Then I just try to create trust with our crewmembers. I know if they trust me, if they know I'm trying to do the best things I think are in their long-term interest, then they'll be happier and they'll feel like this is a better place to work. The top five tips for landing a job at JetBlue include 1. *Do your homework!* Study JetBlue's history and their current happenings and their five core values, 2. *Know your story:* Be prepared for the interview by reviewing your own challenging situations and how you handled them, 3. *Show your passion:* People at JetBlue are very passionate about the company and what they do. Showing passion for the company and role you are applying for is important, 4. *Be open and honest,* and 5. *Be yourself!* "We are a fun company, and we just want you to be you!"[15]

Ethical companies may also include a "social mission" in their formal mission and values statements. A social mission is a commitment by the organization to give back to their community and external stakeholders who make the organization's existence possible. Ben and Jerry's (now a division of the Anglo-Dutch Unilever conglomerate), Lands' End, Southwest Airlines, and many other companies commit to serving their communities through different types of stewardship outreach, facility sharing (e.g., day care and tutoring programs), and other service-related activities.

A starting point for identifying a leader's values is a foundational vision and mission statement of the company. Levi Strauss & Co.'s, shown in Figure 6.2, exemplifies an inspirational vision with ethical values.

The classical visionary, "built-to-last" companies "are premier institutions—the crown jewels—in their industries—several are still 'lasting' today—widely admired by their peers, and have a long track record of making a significant impact on the world around them . . . a visionary company is an *organization*—an institution . . . visionary *companies* prosper over long periods of time, through multiple product life cycles and multiple generations of active leaders."[16] Such companies include 3M, American Express, Boeing, Citicorp, Ford, General Electric, Hewlett-Packard, IBM, Johnson & Johnson, Marriott, Merck, Motorola, Nordstrom, Philip Morris, Procter and Gamble, Sony, Wal-Mart, and Disney. These visionary companies, Collins and Porras discovered, succeeded over their rivals by developing and following a "core ideology" that consisted of core values plus purpose. Core values are "the organization's essential and enduring tenets—a small set of general guiding principles; not to be confused with specific cultural or operational practices; not to be compromised for financial gain or short-term expediency." Purpose is "the organization's fundamental reasons for existence beyond just making money—a perpetual guiding star on the horizon; not to be confused with specific goods or business strategies."[17] Excerpts of core ideologies from some of the classic visionary companies are instructive and are summarized here:[18]

Figure 6.2

Levi Strauss & Co. Values and Vision Statement

VALUES

Our values are fundamental to our success. They are the foundation of our company, define who we are and set us apart from the competition. They underlie our vision of the future, our business strategies and our decisions, actions and behaviors. We live by them. They endure.

Four core values are at the heart of Levi Strauss & Co.: Empathy, Originality, Integrity and Courage. These four values are linked. As we look at our history, we see a story of how our core values work together and are the source of our success.

Empathy—Walking in Other People's Shoes

Empathy begins with listening . . . paying close attention to the world around us . . . understanding, appreciating and meeting the needs of those we serve, including consumers, retail customers, shareholders and each other as employees.

Levi Strauss and Jacob Davis listened. Jacob was the tailor who, in the 1870s, first fashioned heavy cotton cloth, thread and metal rivets into sturdy "waist overalls" for miners seeking durable work pants. Levi in turn met Jacob's needs for patenting and mass production of the product, enthusiastically embracing the idea and bringing it to life. The rest is history: The two created what would become the most popular clothing in the world—blue jeans.

Our history is filled with relevant examples of paying attention to the world around us. We listened. We innovated. We responded.

- As early as 1926 in the United States, the company advertised in Spanish, Portuguese and Chinese, reaching out to specific groups of often-neglected consumers.
- In the 1930s, consumers complained that the metal rivets on the back pockets of our jeans tended to scratch furniture, saddles and car seats. So we redesigned the way the pockets were sewn, placing the rivets underneath the fabric.
- In 1982, a group of company employees asked senior management for help in increasing awareness of a new and deadly disease affecting their lives. We quickly became a business leader in promoting AIDS awareness and education.

We believe in empathetic marketing, which means that we walk in our consumers' shoes. In the company's early years, that meant making durable clothes for workers in the American West. Now, it means responding to the casual clothing needs of a broad range of consumers around the world. Understanding and appreciating needs—consumer insight—is central to our commercial success.

Being empathetic also means that we are inclusive. Levi Strauss' sturdy work pants are sold worldwide in more than 80 countries. Their popularity is based on their egalitarian appeal and originality. They transcend cultural boundaries. Levi's® jeans—the pants without pretense—are not just for any one part of society. Everyone wears them.

Inclusiveness underlies our consumer marketing beliefs and way of doing business. We bring our Levi's® and Dockers® brands to consumers of all ages and lifestyles around the world. We reflect the diverse world we serve through the range and relevancy of our products and the way we market them.

Likewise, our company workforce mirrors the marketplace in its diversity, helping us to understand and address differing consumer needs. We value ethnic, cultural and lifestyle diversity. And we depend and draw upon the varying backgrounds, knowledge, points of view and talents of each other.

As colleagues, we also are committed to helping one another succeed. We are sensitive to each other's goals and interests, and we strive to ensure our mutual success through exceptional leadership, career development and supportive workplace practices.

Empathy also means engagement and compassion. Giving back to the people we serve and the communities we operate in is a big part of who we are. Levi Strauss was both a

Figure 6.2 *–continued*

merchant and a philanthropist–a civic-minded leader who believed deeply in community service. His way lives on. The company's long-standing traditions of philanthropy, community involvement and employee volunteerism continue today and contribute to our commercial success.

Originality–Being Authentic and Innovative

Levi Strauss started it and forever earned a place in history. Today, the Levi's® brand is an authentic American icon, known the world over.

Rooted in the rugged American West, Levi's® jeans embody freedom and individuality. They are young at heart. Strong and adaptable, they have been worn by generations of individuals who have made them their own. They are a symbol of frontier independence, democratic idealism, social change and fun. Levi's® jeans are both a work pant and a fashion statement–at once ordinary and extraordinary. Collectively, these attributes and values make the Levi's® brand unlike any other.

Innovation is the hallmark of our history. It started with Levi's® jeans, but that pioneering spirit permeates all aspects of our business-innovation in product and marketing, workplace practices and corporate citizenship. Creating trends. Setting new standards. Continuously improving through change. For example:

- We were the first U.S. apparel company to use radio and television to market our products.
- With the introduction of the Dockers® brand in 1986, we created an entirely new category of casual clothing in the United States, bridging the gap between suits and jeans. A year later, Dockers® khakis had become the fastest growing apparel brand in history. Throughout the 1990s, we were instrumental in changing what office workers wear on the job.
- Our European Levi's® brand team reinvented classic five-pocket jeans in 1999. Inspired by the shape and movement of the human body, Levi's® Engineered Jeans™ were the first ergonomically designed jeans.

Now, more than ever, constant and meaningful innovation is critical to our commercial success. The worldwide business environment is fiercely competitive. Global trade, instantaneous communications and the ease of market entry are among the forces putting greater pressure on product and brand differentiation. To be successful, it is imperative that we change, competing in new and different ways that are relevant to the shifting times.

As the "makers and keepers" of Levi Strauss' legacy, we must look at the world with fresh eyes and use the power of ideas to improve everything we do across all dimensions of our business, from modest improvements to total reinventions. We must create product news that comes from the core qualities of our brands–comfort, style, value and the freedom of self-expression–attributes that consumers love and prefer.

Integrity–Doing the Right Thing

Ethical conduct and social responsibility characterize our way of doing business. We are honest and trustworthy. We do what we say we are going to do.

Integrity includes a willingness to do the right thing for our employees, brands, the company and society as a whole, even when personal, professional and social risks or economic pressures confront us. This principle of responsible commercial success is embedded in the company's experience. It continues to anchor our beliefs and behaviors today, and is one of the reasons consumers trust our brands. Our shareholders expect us to manage the company this way. It strengthens brand equity and drives sustained, profitable growth and superior return on investment. In fact, our experience has shown that our "profits through principles" approach to business is a point of competitive advantage.

(continued)

Figure 6.2 *–continued*

This values-based way of working results in innovation:

- Our commitment to equal employment opportunity and diversity predates the U.S. Civil Rights movement and federally mandated desegregation by two decades. We opened integrated factories in California in the 1940s. In the 1950s, we combined our need for more production and our desire to open manufacturing plants in the American South into an opportunity to make change: We led our industry by sending a strong message that we would not locate new plants in Southern towns that imposed segregation. Our approach changed attitudes and helped to open the way for integration in other companies and industries.
- In 1991, we were the first multinational company to develop a comprehensive code of conduct to ensure that individuals making our products anywhere in the world would do so in safe and healthy working conditions and be treated with dignity and respect. Our Terms of Engagement are good for the people working on our behalf and good for the long-term reputation of our brands.

Trust is the most important value of a brand. Consumers feel more comfortable with brands they can trust. Increasingly, they are holding corporations accountable, not only for their products but also for how they are made and marketed. Our brands are honest, dependable and trusted, a direct result of how we run our business.

Integrity is woven deeply into the fabric of our company. We have long believed that "Quality Never Goes Out of Style." Our products are guaranteed to perform. We make them that way. But quality goes beyond products: We put quality in everything we do.

Courage—Standing Up for What We Believe

It takes courage to be great. Courage is the willingness to challenge hierarchy, accepted practices and conventional wisdom. Courage includes truth telling and acting resolutely on our beliefs. It means standing by our convictions. For example:

- It took courage to transform the company in the late 1940s. That was when we made the tough decision to shift from dry goods wholesaling, which represented the majority of our business at the time, and to focus instead on making and selling jeans, jean jackets, shirts and Western wear. It was a foresighted–though risky–decision that enabled us to develop and prosper.
- In the 1980s, we took a similar, bold step to expand our U.S. channels of distribution to include two national retail chains, Sears and JCPenney. We wanted to provide consumers with greater access to our products. The move resulted in lost business in the short term because of a backlash from some important retail customers, but it set the stage for substantial growth.
- We also demonstrated courage in our workplace practices. In 1992, Levi Strauss & Co. became the first Fortune 500 company to extend full medical benefits to domestic partners of employees. Although controversial at the time, this action foreshadowed the widespread acceptance of this benefit and positioned us as a progressive employer with prospective talent.

With courage and dedication, we act on our insights and beliefs, addressing the needs of those we serve in relevant and significant ways. We do this with an unwavering commitment to excellence. We hold ourselves accountable for attaining the high performance standards and results that are inherent in our goals. We learn from our mistakes. We change. This is how we build our brands and business. This is how we determine our own destiny and achieve our vision of the future.

The story of Levi Strauss & Co. and our brands is filled with examples of the key role our values have played in meeting consumer needs. Likewise, our brands embody many of the core values that our consumers live by. This is why our brands have stood the test of time.

Figure 6.2 *–continued*

Generations of people have worn our products as a symbol of freedom and self-expression in the face of adversity, challenge and social change. They forged a new territory called the American West. They fought in wars for peace. They instigated counterculture revolutions. They tore down the Berlin Wall. Reverent, irreverent–they all took a stand.

Indeed, it is this special relationship between our values, our consumers and our brands that is the basis of our success and drives our core purpose. It is the foundation of who we are and what we want to become:

Vision

People love our clothes and trust our company.
We will market the most appealing and widely worn casual clothing in the world.
We will clothe the world.

Source: Levi Strauss & Co. Used by permission of Levi Strauss & Co. Reprinted by permission of Levi Strauss & Co.

- Disney: "To bring happiness to millions and to celebrate, nurture, and promulgate wholesome American values."
- Wal-Mart: "We exist to provide value to our customers—to make their lives better via lower prices and greater selection; all else is secondary. . . . Be in partnership with employees."
- Sony: "Respecting and encouraging each individual's ability and creativity."
- Motorola: "To honorably serve the community by providing products and services of superior quality at a fair price."

Built-to-last companies "more thoroughly indoctrinate employees into a core ideology than their comparison companies [i.e., those companies in Collins and Porras's study that did not last], creating cultures so strong that they are almost cult-like around the ideology."[19] Visionary companies also select and support senior management on the basis of whether they fit with the core ideology. These best-in-class companies also attain more consistent goals, strategy, and organizational structure alignment with their core ideology than do comparison companies in Collins and Porras's study.[20]

Ethical Insight 6.1

Your Moral Leadership Profile

Using actual situations in which you served in a leadership role, score the following statements with regard to how each statement characterizes your leadership style:

1 = Very little, 2 = Somewhat, 3 = Moderately, 4 = A lot, 5 = Most of the time

1. I act ethically even if my peers disagree with me. 1 2 3 4 5
2. I generally speak out for what I believe is right regardless of pressure from others. 1 2 3 4 5

3. I tell others when I sense there are wrongdoing or hurtful activities about to happen. 1 2 3 4 5
4. I maintain composure when people try to pressure me into saying or doing unjust things. 1 2 3 4 5
5. I do not back down when I know that others are violating just rules and procedures. 1 2 3 4 5
6. I don't go along with the crowd or majority just to get their approval when I know they are wrong and/or acting unethically. 1 2 3 4 5
7. My decisions are generally ethical and based on principles, not on random acts of instant gratification or whim. 1 2 3 4 5
8. I say and do the right thing even if I lose the favor of some friends. 1 2 3 4 5
9. I generally act from my beliefs and ethical principles first, regardless of the approval of my friends. 1 2 3 4 5
10. I go with what's right for a project even though my friends and colleagues may turn against me. 1 2 3 4 5

Your Scores and Interpretation

Add up your scores. Total of 10 statements = ____. If you received 40 or higher, you are considered a courageous leader. A score of 20 or below indicates you avoid conflict and difficult situations that challenge your moral leadership. Examine the items in which you scored highest and lowest. Do these scores and items reflect your moral courage in tough situations generally? Why or why not? What do you need to do to improve or change your moral courage? How do your scores compare to other students?

Source: Adapted from *The leadership experience*, 3rd edition by Daft. © 2005, South-Western, a division of Thomson Learning.

Leadership Stakeholder Competencies

Core competencies of responsible leaders include the ability to:

1. Define and lead the social, ethical, and competitive mission of organizations. This includes community-based, social, and environmental stewardship goals that promote being a global corporate citizen.[21]
2. Build and sustain accountable relationships with stakeholders.[22]
3. Dialogue and negotiate with stakeholders, respecting their interests and needs beyond economic and utilitarian dimensions.[23]
4. Demonstrate collaboration and trust in shared decision making and strategy sessions.
5. Show awareness and concern for employees and other stakeholders in the policies and practices of the company.

Effective ethical leaders develop a collaborative approach to setting direction, leading top-level teams, and building relationships with partners and

customers. For example, at Johnson & Johnson, one of the seven principles of leadership development states: "People are an asset of the corporation; leadership development is a collaborative, corporation-wide process."[24] The company lives its leadership principles through its Executive Development Program. Figure 6.3 shows Johnson & Johnson's Credo. The now classic "Beliefs of BorgWarner" corporation credo is shown in Figure 6.4 as another example of values companies should aspire to follow.

Organizational leaders are also ultimately responsible for the economic viability and profitability of a company. From a values-based, stakeholder management perspective, leaders must also oversee and implement the following in their organizations:

Figure 6.3

Johnson & Johnson Credo

We believe our first responsibility is to the doctors, nurses, and patients; to mothers and fathers; and all others who use our product and services. In meeting their needs, everything we do must be of high quality.

We must constantly strive to reduce our costs in order to maintain reasonable prices.

Customers' orders must be serviced promptly and accurately.

Our suppliers and distributors must have an opportunity to make a fair profit.

We are responsible to our employees, the men and women who work with us throughout the world.

Everyone must be considered as an individual. We must respect their dignity and recognize their merit.

They must have a sense of security in their jobs.

Compensation must be fair and adequate, and working conditions clean, orderly, and safe.

We must be mindful of ways to help our employees fulfill their family responsibilities.

Employees must feel free to make suggestions and complaints.

There must be equal opportunity for employment, development, and advancement for those qualified.

We must provide competent management, and their actions must be just and ethical.

We are responsible to the communities in which we work and to the world community as well.

We must be good citizens–support good works and charities and bear our fair share of taxes.

We must encourage civic improvements and better health and education.

We must maintain in good order the property we are privileged to use, protecting the environment and natural resources.

Our final responsibility is to our stockholders.

Business must make a sound profit.

We must experiment with new ideas.

Research must be carried on, innovative programs developed, and mistakes paid for.

New equipment must be purchased, new facilities provided, and new products launched.

Reserves must be created to provide for adverse times.

When we operate according to these principles, the stockholders should realize a fair return.

Source: Johnson & Johnson. Reprinted by permission of Johnson & Johnson.

- Set the vision, mission, and direction.
- Create and sustain a legal and ethical culture throughout the organization.
- Articulate and guide the strategy and direction of the organization.
- Ensure the competitive and ethical alignment of organizational systems.
- Reward ethical conduct.[25]

Herb Kelleher cofounded Southwest Airlines in 1966 on a personal $10,000 investment. He retired June 19, 2001, with a $200 million stake in the company. Kelleher's principles of management are straightforward and simple:[26]

- Employees come first, customers second.
- The team is important, not the individual.
- Hire for attitude, train for skills.
- Think like a small company.
- Eschew organizational hierarchy.
- Keep it simple.

Kelleher owned and operated Southwest Airlines on these principles. When asked how the company would survive once he stepped down, Kelleher responded, "The real answer is we have a very strong culture and it has a life of its own that is able to surmount a great deal. If we should, by happenstance, have someone succeed me who is not interested in the culture, I don't think they would last a long time. The place would just rise up."[27] Kelleher's message is printed in white letters on the black elevator glass in the lobby of Southwest's corporate headquarters: "The people of Southwest Airlines are the creators of what we have become—and what we will be. Our people transformed an idea into a legend. That legend will continue to grow only so long as it is nourished—by our people's indomitable spirit, boundless energy, immense goodwill, and burning desire to excel. Our thanks—and our love—to the people of Southwest Airlines for creating a marvelous family and a wondrous airline."[28]

Leaders who dare to be different stretch goals while maintaining a moral, values-based approach:

- Seek to revolutionize every strategy and process for optimal results while maintaining the organization's integrity.[29]
- Empower everyone to perform beyond stated standards, while maintaining balance of life and personal values.
- Understand and serve customers as they would themselves.
- Create and reward a culture obsessed with fairness and goodwill toward everyone.
- Act with compassion and forgiveness in every decision toward every person and group.
- Do unto their stockholders and stakeholders as they would have them do to their company.
- Treat the environment as their home.

Figure 6.4

The Beliefs of BorgWarner: To Reach beyond the Minimal

Any business is a member of a social system, entitled to the rights and bound by the responsibilities of that membership. Its freedom to pursue economic goals is constrained by law and channeled by the forces of a free market. But these demands are minimal, requiring only that a business provide wanted goods and services, compete fairly, and cause no obvious harm. For some companies, that is enough. It is not enough for BorgWarner. We impose upon ourselves an obligation to reach beyond the minimal. We do so convinced that by making a larger contribution to the society that sustains us, we best assure not only its future vitality, but our own.

This is what we believe.

We Believe in the Dignity of the Individual

However large and complex a business may be, its work is still done by dealing with people. Each person involved is a unique human being, with pride, needs, values, and innate personal worth. For BorgWarner to succeed, we must operate in a climate of openness and trust, in which each of us freely grants others the same respect, cooperation, and decency we seek for ourselves.

We Believe in Our Responsibility to the Common Good

Because BorgWarner is both an economic and social force, our responsibilities to the public are large. The spur of competition and the sanctions of the law give strong guidance to our behavior, but alone do not inspire our best. For that we must heed the voice of our natural concern for others. Our challenge is to supply goods and services that are of superior value to those who use them; to create jobs that provide meaning for those who do them; to honor and enhance human life; and to offer our talents and our wealth to help improve the world we share.

We Believe in the Endless Quest for Excellence

Though we may be better today than we were yesterday, we are not as good as we must become. BorgWarner chooses to be a leader–in serving our customers, advancing our technologies, and rewarding all who invest in us their time, money, and trust. None of us can settle for doing less than our best, and we can never stop trying to surpass what already has been achieved.

We Believe in Continuous Renewal

A corporation endures and prospers only by moving forward. The past has given us the present to build on. But to follow our visions to the future, we must see the difference between traditions that give us continuity and strength and conventions that no longer serve us–and have the courage to act on that knowledge. Most can adapt after change has occurred; we must be among the few who anticipate change, shape it to our purpose, and act as its agents.

We Believe in the Commonwealth of BorgWarner and Its People

BorgWarner is both a federation of businesses and a community of people. Our goal is to preserve the freedom each of us needs to find personal satisfaction, while building the strength that comes from unity. True unity is more than a melding of self-interests; it results when values and ideals also are shared. Some of ours are spelled out in these statements of belief. Others include faith in our political, economic, and spiritual heritage; pride in our work and our company; the knowledge that loyalty must flow in many directions; and a conviction that power is strongest when shared. We look to the unifying force of these beliefs as a source of energy to brighten the future of our company and all who depend on it.

Source: BorgWarner Corp. Reprinted by permission of the BorgWarner Corporation.

Example of Companies Using Stakeholder Relationship Management

A recent study of exemplary companies that have gone beyond traditional business models coined the term "firms of endearment" (FoE), which is explained in Case 9 in Chapter 4. Leaders of these firms practice "stakeholder relationship management."[30] An FoE is "a company that *endears* itself to stakeholders by bringing the interests of all stakeholder groups into strategic alignment. No stakeholder group benefits at the expense of any other stakeholder group, and each prospers as the others do."[31] The authors' (Sisodia, Sheth, and Wolfe) two-year research project started with measures of "humanistic performance—meeting the needs of stakeholders other than shareholders—and worked forward." The authors "asked for nominations from thousands of people all over the world, including business professionals, marketing professionals, MBA students, and about 1,000 consumers."[32] The companies selected underwent further screening using quantitative and qualitative performance of each firm for each stakeholder (societal communities, partners, investors, customers, and employees). The companies studied are not exhaustive, and the authors note that none of the firms are perfect. It was found that "the public FoEs returned 1,026% for investors over the 10 years ending June 30, 2006, compared to 122% for the S&P 500 . . . an 8–1 ratio!"[33] The companies in the "final cut" include:

Amazon	Honda	Southwest
BMW	IDEO	Starbucks
CarMax	IKEA	Timberland
Caterpillar	JetBlue	Toyota
Commerce Bank	Johnson & Johnson	Trader Joe's
The Container Store	Jordan's Furniture	UPS
Costco	LL Bean	Wegmans
eBay	New Balance	Whole Foods
Google	Patagonia	
Harley-Davidson	REI	

Some of the defining characteristics of FoEs include:

- Competitive advantage through a business model in which all stakeholders add and benefit from gains in value created from a deeper set of resources.
- Possess a humanistic soul. "From the depths of this soul, the will to render uncommon service to all stakeholders flows. These companies are imbued with the joy of service—to the community, to society, to the environment, to customers, to colleagues."[34]
- Leaders who "facilitate, encourage, reward, recognize, and celebrate their employees for being of service to their communities and the world at large, for no reason other than that it is the right thing to do."[35]

Honda, for example, "marries suppliers for life"; the company supports suppliers in improving quality, service, and profits. IKEA abides by all laws, no matter how strict, in every country where it operates. Costco's cofounder and CEO Jim Sinegal embodies the stakeholder management approach. His salary for the fiscal year 2011 was $350,000, with a bonus of $198,400; Costco's revenues in its most recent fiscal year rose 14% to $88.92 billion. (The average CEO compensation of a Forbes 500 company in 2010 was $9 million.[36]) Costco's low employee turnover and liberal benefits have created loyalty in an industry that is standard-setting. Southwest Airlines has an elected "Culture Committee" consisting of 96 employees in charge of sustaining the company's humanistic culture. JetBlue's founder, David Neeleman, quickly responded to the post-2007 Valentine's Day crisis when passengers were kept on board planes that had been grounded due to weather conditions. Neeleman instituted "employee cross-training so that all 900 of the corporate employees in JetBlue's Forest Hills office could assist at nearby JFK during any future operational crisis."[37] Neeleman also initiated action on a customer's "Bill of Rights" document. All the FoE companies and their leaders exhibited these types of stakeholder relationship management actions, attributes, and policies.

Ethical Insight 6.2

Global CEO Survey: Leaders CEOs Most Admire

PricewaterhouseCoopers' (PWC) annual survey asked CEOs in 60 countries "to share an example of someone from literature or history who exhibited good leadership, and what the CEOs admired about them." PWC was interested in the types of leaders CEOs named and reasons for naming them. The top 10 people named by CEOs across seven regions and over 60 countries were:

1. Winston Churchill
2. Steve Jobs
3. Mahatma Gandhi
4. Nelson Mandela
5. Jack Welch
6. Abraham Lincoln
7. Margaret Thatcher
8. Ronald Reagan
9. John F. Kennedy
10. Bill Clinton/Napoleon Bonaparte

There was an unusually high degree of agreement on leaders admired across different geographies and cultures. CEOs identified Winston Churchill in 30 countries across six regions. Steve Jobs was identified by CEOs in 37 countries and six regions. PWC also discovered that CEOs named by emerging-market countries tended to identify role models in regions other than their own, even though they gave tribute to local heroes. North

American and Western European CEOs were more alike in their choices and chose most admired leaders nearer home. PWC noted this finding indicated that these CEOs might "reflect their markets' dominant economic standing in recent history—but could also be an obstacle to their ability to adapt to different cultural traits that are gaining (or regaining) prominence as the global economy rebalances." Fifteen female leaders were identified, and Margaret Thatcher was the only one in the top 10 who received several mentions. Next most identified were Angela Merkel, Ayn Rand, Mother Teresa, and Queen Elizabeth I. The authors found that "Female CEOs were more than four times more likely to select female leaders than male CEOs: 17% of women CEOs chose women leaders, with 78% choosing male leaders. 4% of male CEOs, meanwhile, named female leaders and 95% named male leaders." Leaders who had "a strong vision" were most identified. Other characteristics included "motivational, caring, innovative, persistent and ethical qualities." Respondents seemed to choose leaders who were driven "by the prevailing mood of the time, which could explain why so many CEOs chose leaders who were persistent in the face of adversity—as well as transformational leaders and leaders who did the 'right thing.'"

Questions

1. Who are your most admired leaders?
2. What traits do/did they have?
3. How would you describe and characterize their ethics?
4. How alike and/or different are your choices from your (evolving) leadership style? Explain.

Source: PricewaterhouseCoopers. (2013). Global CEO survey: Leaders CEOs most admire. *PWC.com.* http://www.pwc.com/gx/en/ceo-survey/2013/key-findings/admired-leaders-leadership-attributes.jhtml, accessed January 8, 2014.

Spiritual Values, Practices, and Moral Courage in Leading

John Kotter of Harvard University has said that "What we call courage is a strong emotional commitment—and the keyword is emotional—to some ideas. Those ideas could be called a vision for where we're trying to drive the enterprise. They could be called values for what we think is important in life. They could be called principles of what is right and wrong. When people don't just have an intellectual sense that these are logically good, but are deeply committed to them, they're developing courage. When you run up against barriers that keep you from those ideals, the stronger your commitment, the more likely you are to take action consistent with those ideals. Even if it's against your short-term best interests. . . . The bigger the context, the greater the barriers, the more the snake pits . . . the more there will be times for courageous acts."[38]

Moral courage comes from the heart and soul as well as the head. When leaders face extreme dilemmas, where not only their own but their organiza-

tion's reputation or existence is at stake based on the course of action that must be taken (or not taken), they come to know the meaning of this type of courage. An emerging body of literature describes leadership from just such a spiritual perspective.[39] Spirituality, broadly defined, is the search for "ultimate meaning and purpose in one's life."[40] This dimension of leadership is inherently linked to ethics, in that leaders act as stewards and servants who do "the right thing" for their followers, communities, and society.[41] Spiritual values and practices are also the sources of moral courage, which is the ability to act with wisdom of the soul against fear, greed, conformity, and pressures that work against the common good. Spiritual values originate from a deeper wisdom of having a sense of purpose and "knowing yourself." Some religious traditions, including Christianity, link this deeper knowing to a person's "calling" that is discovered and nurtured from their relationship with community and the source of their spiritual guidance. The following characteristics illustrate leadership from a spiritual perspective:[42]

- Understand and practice reflective "being" as well as "doing"; genuine spirituality must be the willingness to enter into the process of dialogue with oneself and with others, and to try to stay with it over a period of time. "Being is the only reality with integrity; obeying one's conscience brings one into communion with this 'integrity of Being.' "[43]
- Use discernment, prayer, and patience in strategic decision making. Decisions are analyzed within the context of communities.
- See the leadership role as a calling that reveals its presence by the enjoyment and sense of renewed energy in the practice and results yielded.
- Seek to connect with people and connect people to people with meaning and in meaningful ways.
- Create communities, environments, and safe havens for empowerment, mobilization, development, spiritual growth, and nourishment.
- Lead with reflection, choice, passion, reason, compassion, humility, vulnerability, and prayer, as well as courage, boldness, and vision.

Spiritually based values and practices of leaders have been shown to positively affect their stakeholder relationships as well as performance: "The spiritual values of integrity, honesty, and humility, and the spiritual practices of treating others with respect and fairness, expressing caring and concern, listening responsively, appreciating others, and taking time for personal reflection have all been linked to quantifiable positive effects for organizations and individuals. They cause leaders to be judged as more effective by both their peers and their subordinates, and they lead to enhanced performance. They have been proven to be associated with increased worker satisfaction and motivation, greater productivity, greater sustainability, and enhanced corporation reputation, which in turn have all been linked to increases in the bottom line of profits."[44]

Jim Collins's Level 5 leadership, or servant leadership, focuses on ethical behavior through good stewardship. Leaders that act as stewards both empower followers in their decision making and help them gain control over their work. Servant leadership is selfless and involves working alongside followers to achieve shared goals and improve collective welfare. The focus is not on the individual, but on the whole. A key component of ethical leadership is the treatment of followers with respect, empowering them to grow both personally and professionally. Servant leaders lead with respect and empowerment.

Leading with stewardship assumes an authority without domination. These leaders sincerely care for their followers' well-being and achievement of personal and professional goals. This kind of effective stewardship results in a team-oriented, cooperative environment. Organizations led by stewardship are often characterized by decentralized decision-making structures. Authority is not centered in a single individual, group, department, or administrative body, distributing power among all stakeholders. James Goodnight, CEO of SAS Institute; Ed Bastian, president of Delta Airlines; Herb Kelleher, former CEO and cofounder of Southwest; Aaron Feuerstein, founder of Malden Mills Industries, Inc.; Tom Chappell of Tom's of Maine; Jeffrey Swartz of the Timberland Company; David Steward of World Wide Technology, Inc.; and Krishan Kalra of BioGenex Laboratories, Inc. are some leaders—past and present—who have relied on their spiritual beliefs in their professional lives to create and promote strategies and policies involving employees, customers, suppliers, vendors, their communities, and other stakeholders. JetBlue's founder David Neeleman also admitted that his Mormon background and "missionary" responsibilities as a youth influenced his continuing values and practices toward his employees and stakeholders.

The servant leadership approach implemented by the leaders listed above, among many others, was formulated by Robert K. Greenleaf. Greenleaf saw a strong correlation between leadership and service, stating that "the essential quality that separates servant-leaders from others is that they live by their conscience—the inward moral sense of what is right and wrong. That one quality is the difference between leadership that *works* and leadership – like servant leadership—that endures." Stewardship demands that leaders devote themselves to a greater cause, rather than personal accolades. This approach to leadership is characterized by the following attributes:

1. *Placing service before self-interest*: Recognition or financial rewards are not the primary concern of servant leaders.
2. *Listening to others*: Servant leaders do not impose their will on others, but listen to the concerns and ideas of all stakeholders. This strengthens relationships, provides an understanding of group dynamics and needs, and allows for more effective allocation of resources.
3. *Inspiring followers through trust*: Servant leaders value trust and are truthful, due to their strong moral convictions.
4. *Working toward feasible goals*: Problem solving is most often a team effort, and servant leaders work toward solving the most pressing issues.

5. *Helping others whenever possible*: Servant leaders go out of their way to help those around them; often these above and beyond tasks are not an explicit part of their job description.

Stewardship and servant leadership are targeted at empowering followers to become champions. They often evoke strong loyalty and cooperation in and out of the workplace. The ethical style of these leaders is one of universalism, altruism, and pragmatism. They demonstrate Kouzes and Posner's five dimensions of transformational leadership: ethically modeling the way; inspiring a shared vision; challenging the process; enabling others to act; and encouraging the heart in ways that exceed transactional, transformational, and charismatic leaders.[45] DeGraaf, Tilley and Neal discuss servant leadership as follows: "The main assumption is that true leadership should call us to serve a higher purpose, something beyond ourselves. One of the most important aspects of leadership is helping organizations and staff identify their higher purpose. The best test of the Servant-Leadership philosophy is whether or not customers and staff grow as persons! Do customers become healthier, wiser, free, more autonomous, more likely themselves to become 'servants'? And, what is the effect on the least privileged in society? Will they benefit? Or, at least, not be further deprived? To achieve this higher purpose of public organizations, you, as a leader, must be passionate about your desire to improve your community and yourself!" As stakeholders increasingly value social responsibility and broaden its application to business practices, ethical leadership will remain relevant and become an even more significant matter.[46]A study by Mitroff and Denton interviewed 215 executive officers and managers.[47] A surprising finding was that the leaders desired a way to express their spiritual selves while at work, rather than to "park it at the office door." Leaders and organizations enable the expression of spirituality in different ways: from the *religious firm,* where religious teachings are openly articulated, modeled, and included in business practices, to the *values-based company* (like Ben & Jerry's), where secular values (awareness, consciousness, dignity, honesty, openness, and trust) are guides in the firm. In these types of firms, the Golden Rule is the major business principle and "the whole person comes to work" and "causes no embarrassment by expressing 'deeply felt emotions' such as love and grieving."[48]

Failure of Ethical Leadership

Corporate leaders can and do fail when their decisions lack moral courage. The examples and cases in this text regarding U.S. corporate scandals clearly demonstrate that corruption started at the top. There are also classic scenarios of leaders who violated their legal and ethical responsibilities to stockholders and stakeholders. Mickey Monus, former CEO of the Phar-Mor company (a failed discount retail drugstore chain that attempted to take on Wal-Mart), was sentenced to 20 years in prison and fined $1 million on December 12, 1995, when he was "convicted on all counts of a 109-count indictment that charged him with conspiracy to commit mail fraud, wire

fraud, bank fraud, and transportation of funds obtained by theft or fraud." Monus was hailed as a community hero in Youngstown, Ohio, when he led Phar-Mor to historical growth. But his charismatic, entrepreneurial personality and leadership had a dark side—greed, deceit, and theft. His influence also led his young finance management team into massive theft, fraud, and cover-up.[49]

There was also "Chainsaw Al" Dunlap, former CEO of Sunbeam, who was fired following a Securities and Exchange Commission investigation of accounting fraud under his watch. Dunlap was known for his ability to achieve profits. To meet Sunbeam's profit projections and appease Wall Street analysts, Dunlap devised a method of selling Sunbeam spare parts (used to fix broken blenders and grills) for $11 million to a company that warehoused the parts. That company valued the parts at $2 million. Dunlap and company pressured the warehouse firm to sign a contract to buy the parts at $11 million, booking $8 million in profit. (The parts were never sold.) He was instrumental in laying off large numbers of employees and cutting back organizational operations to achieve profitability.[50] Dunlap described his other approaches to doing business in his book *Mean Business: How I Save Bad Companies and Make Good Companies Great*.[51]

Seven symptoms of the failure of ethical leadership provide a practical lens to examine a leader's shortsightedness:[52]

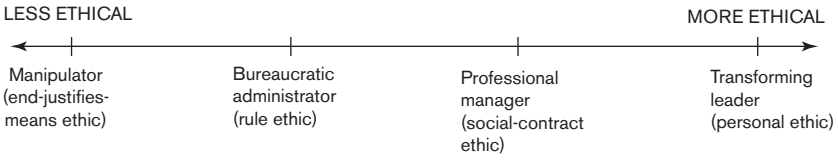
1. Ethical blindness: They do not perceive ethical issues due to inattention or inability.
2. Ethical muteness: They do not have or use ethical language or principles. They "talk the talk" but do not "walk the talk" on values.
3. Ethical incoherence: They are not able to see inconsistencies among values they say they follow; e.g., they say they value responsibility, but reward performance based only on numbers.
4. Ethical paralysis: They are unable to act on their values from lack of knowledge or fear of the consequences of their actions.
5. Ethical hypocrisy: They are not committed to their espoused values. They delegate things they are unwilling to or cannot do themselves.
6. Ethical schizophrenia: They do not have a set of coherent values; they act one way at work and another way at home.
7. Ethical complacency: They believe they can do no wrong because of who they are. They believe they are immune to being unethical.

Ethical Dimensions of Leadership Styles

Every leadership style has an ethical dimension. The following spectrum of styles is illustrated here because it reflects some of the ethical principles discussed in Chapter 2. An organizational leader's (as well as your own) moral decision-making style can also be evaluated using the continuum shown in Figure 6.5.[53]

Figure 6.5

Moral Leadership Styles



The *manipulator* leadership style is based on a Machiavellian principle that views leadership amorally. That is, the end result justifies the means taken to reach it. Power is the driving force behind a manipulator's motives. This is an egotistically and essentially economically motivated moral leadership style. Leaders who lack trust and interest in relationship building and are oriented toward the short term may also be manipulators. Although the motives underlying this style may be amoral, the consequences could prove immoral. Have you ever worked under someone who used this style?

The *bureaucratic administrator* is a rule-based moral leadership style. Based on the theories of German sociologist Max Weber, the bureaucratic administrator acts on the rational principles embodied in an ideal organizational bureaucracy, that is, fixed rules that explain the purpose and functions of the organization, a hierarchy that shows the chain-of-command, well-defined job descriptions, professional managers who communicate and enforce the rules, and technically qualified employees who are promoted by expertise and rewarded by rank and tenure.[54] The driving force behind this style is efficiency ("doing things right," functioning in the least wasteful manner) more than effectiveness (producing the intended result or aim, "doing the right things"). Although this leadership style has an admirable aim of basing decisions only on objective, rational criteria, the moral problem with it lies in the "sin of omission." That is, a leader may follow all the rules exactly but hurt someone unintentionally by not attending to legitimate human needs because the option to do so was not included in the rules.

For example, a military captain may follow remote orders of a general by sending a regiment into a battle zone that he knows will lead to disaster based on available "on the ground" conditions. Nevertheless, rather than risk disobeying orders and the formal consequences, he proceeds. Another captain who has a different moral leadership style may choose to risk disobeying orders to save the troops. Rules for overly bureaucratic leaders can become ends in themselves.

Rules cannot address all problems and needs in what we know are imperfect and political organizations. The well-intentioned bureaucratic administrator may try to act amorally, but his or her efforts could result in immoral and irresponsible consequences. Do you recognize this moral leadership style? Have you ever worked for someone who used it?

The *professional* manager aims at effectiveness and "doing things right." This style is grounded in Peter Drucker's view of managers as professionals

who have the expertise and tools for accomplishing work effectively through others.[55] Based on a social contract, this management style relies—like the previous two styles—on amorality for getting work done. For example, professional career managers use rational objectives and their training to accomplish the organization's work. The organization's corporate culture and the social contract—implicit and explicit agreements—made between managers and organizational executives set the ground rules that govern the manager's behavior. However, social contracts are not always ethical.

An ethical problem with this leadership style lies in the real possibility that the collective corporate culture and the dominant governing group may think and act amorally or immorally. *Groupthink* (consensus-dominated decision making, based on uncritical, biased thinking) may occur.[56] The collective may lead itself astray. Professional managers, by training, are still prone to unethical behavior. Do you recognize managers or leaders who act amorally or immorally as "professionals"?

Finally, the *transforming* leadership style, based on James Burns's theory,[57] is grounded on a personal ethic. The transformational leader bases his or her effectiveness on relationships with followers. Also, this style focuses on the charisma, energy, and excitement the leader brings to relationships. The transformational leader is involved in the growth and self-actualization of others and views others according to their potential. This type of leader identifies and elevates the values of others. He or she empowers, coaches, and helps promote other leaders. This leadership style is moral because "it raises the level of human conduct and aspirations of both leaders and led, and thus has a transforming effect on both."[58]

William Hitt moved the continuum of moral leadership one step beyond the transformational leader to what he termed an "encompassing approach to leadership," or "the effective leader–manager."[59] The encompassing leader learns from the shortcomings of each of the four leadership styles on the continuum and uses all of their strengths. For example, manipulative leadership does value the effective use of power. However, this style's deceptive and dysfunctional use of power should be avoided. The bureaucratic administrator values the effective use of rules; however, these should not become ends rather than means. The professional manager values results; however, human concerns should be valued more highly than physical and fiscal results. The transformational leader values human empowerment; however, even this characteristic is not the complete job of management.

Socially and morally responsible leaders should observe their obligations to all stakeholders, including their own conscience, and observe in their dealings the ethical principles of rights, justice, and duty—in addition to utilitarian logic. Richard Branson, founder and chairman of the Virgin Group, is another example of a popular global leader who practices ethical stakeholder management. A partial list of influential actions in 2007 include his Virgin Airlines "blowing the whistle on an illegal airline cargo price collusion and Virgin ponying up a $25 million prize for whomever can develop a commercially viable design to cut down on greenhouse gasses" (Virgin Earth).[60]

Branson noted in a CNN interview, "I would say . . . most important is how good you are with dealing with people, you know, whether you're a good motivator of people. And I think that, no question, that ethics should play a big part, I think, for a company. If you deal well with people and fairly with people, then people will want to continue to deal with you and come back for more." He continued on a related topic about business ethics: "If we'd wanted to fly to a particular country in this world—and I'm not to talk about America—you know, as a country we desperately wanted to fly to, we'd wanted to fly years ago, and we were willing to slip some money under the table, it would have cost next to nothing to get a license to fly to it. We felt that was wrong. And we just wouldn't do something like that. And, therefore, it took us 10 years before we legitimately got the license. And so I think it's very important that you sleep well at night and that you run your company in an ethical way."[61]

How Should CEOs as Leaders Be Evaluated and Rewarded?

CEO Pay: Excessive or Earned?

Fair and just compensation systems for executives and professionals are necessary for creating long-term corporate value, and for encouraging active participation in the legal, ethical, and business effectiveness of firms. Pay and compensation are not the only ways organizational leaders, CEOs in particular, are compensated. There are also intrinsic as well as extrinsic rewards that motivate leaders, especially those who follow the servant and stewardship models. However, many CEOs of large, publicly traded firms are selected and evaluated based on their level of pay and compensation. It is important to reiterate that most CEOs, especially in small, medium, and even large firms, earn their salaries and benefits from the value they create for their companies. And although many have increased the revenue and market value of their firms many times over, there are, however, a large number of CEOs whose pay and compensation drastically exceeds their firm's performance.

Executive compensation is largely a demonstration of accountability. Increasing scrutiny and pressure has been placed on the topic of CEO compensation following global economic difficulties and corporate scandals. The *Wall Street Journal*/HayGroup 2010 CEO Compensation Study noted that pay levels were substantially higher in 2010 than in 2009. "While pay levels showed increases that were in line with company performance improvements, the structure of pay saw meaningful changes, as more companies increased their emphasis on performance-oriented long-term incentive programs, and continued to eliminate some of the 'extras' like executive perquisites." Consider these facts: CEOs made more money in 2010 than in 2011, as the bull market swelled the value of prior stock-based compensation. Executive pay rose a median 3.6% to $10.1 million in 2012, according to that year's *Wall Street Journal*/Hay Group study, which examined CEO pay from the 300 largest U.S. public companies by revenue that filed their definitive proxy statements between May 1, 2012, and April 30, 2013.[62,63]

Several issues are at stake here. First, after the corporate scandals, many investors and the public are more skeptical of CEO pay and performance. Second, many CEOs who have been with the same company most of their careers are looking toward retirement and do not need bonuses or perks that they could well afford on their own. Third, the salary increases, stock options, and perks are offered even when the company's performance is suboptimal and layoffs are occurring. Fourth, the CEO's pay can be 20, 30, or 50 times higher than the salaries of some first-line managers and supervisors. However, a difference of more than a factor of seven is considered sizable for an average CEO position. Finally, although CEOs certainly bear greater responsibility, risk, and blame for a company's successes and failures, one question remains: Why are CEO salaries and perks not linked more to performance? Activist shareholders are beginning to address this question and issue. For example, in 2007, shareholders howled when they discovered that Robert Nardelli's contract as chief of the Home Depot enabled him to command a severance package totaling $210 million when he was ousted. The Home Depot board did not make the same mistake when it wrote the contract for Frank Blake, Nardelli's successor. "Frank Blake's package is so tied to performance that it is almost the mirror image of Nardelli's," said Minow of the Corporate Library. "Home Depot went from the worst pay package imaginable to one that is close to exemplary."[64]

CEO Evaluations

The board of directors of a company is technically responsible for disciplining and rewarding the CEO. This is reflected in the increasing number of board evaluations of the CEO—86% of public company boards perform an annual CEO evaluation, according to a 2009 National Association of Corporate Directors study. "For both nonprofit and investor-owned organizations, appointing the CEO, establishing his or her performance expectations, and assessing the CEO's performance in relation to those expectations are among a governing board's most fundamental and important duties."[65] Evidence shows that "CEO appraisals require a special commitment from the CEO and from the board members" in order for the process to work well and the results to be meaningful. "A CFO magazine survey of 2,000 employees in several large public companies found that only 39% believe their performance reviews are effective."[66] However, in many instances, it is the CEO who is also president of the company and chairperson of the board.

Two forces influence the popularity of boards of directors evaluating CEOs. The first is the increased recognition of the critical roles CEOs play and the increased compensation levels received for those roles. The second influential force is pressure from the investment community, which dates back to the beginning of shareholder awareness in the 1980s, when corporate acquisitions and restructuring activities were questioned with regard to the effectiveness of CEOs and their boards, due diligence, and management practices. Still, not all CEOs are formally evaluated with their top-level team members and other employees. For publicly traded companies, such as those listed on the New York Stock Exchange, NASDAQ, and other trading companies, industry

analysts constantly score and keep pressure on the performance of CEOs and chief financial officers (CFOs)—by the numbers. Market performance is a major evaluator of these officers' effectiveness. Annual reports and financial audits available to stockholders are another form of assessing leaders.

CEOs are also evaluated by assessing gaps between their stated and enacted strategies and by using customer and employee surveys. Assessments of the organization's systems are also reflections of the leader's overall effectiveness in directing, aligning, and implementing strategy. Finally, leaders must balance and align stakeholder interests with the dominant mission and values of the company. Certainly not all CEOs are overpaid. Still, many critics argue that CEO pay and compensation in the larger, publicly traded companies are not in line with the performance of their firms, especially over the last decade.

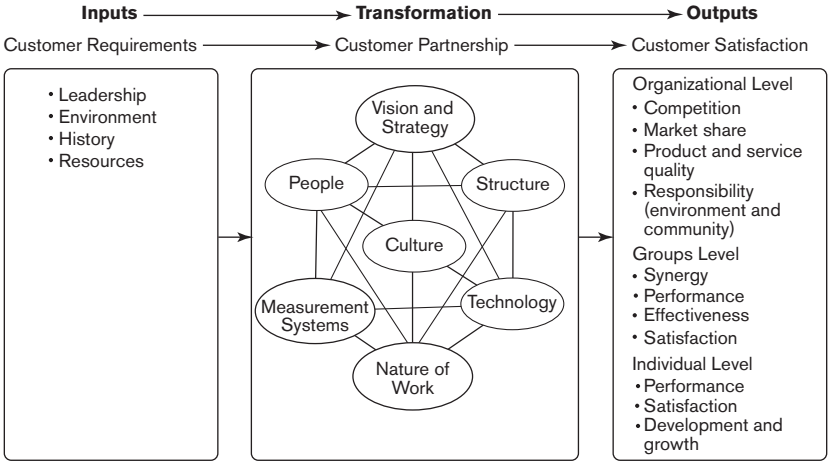
6.2 Organizational Culture, Compliance, and Stakeholder Management

The most recent survey by the Ethics Resource Center (ERC) reported a reduction in the percentage of employees who witnessed misconduct to only 45%. Of those employees, 65% reported the wrongdoing. The survey notes a new and disturbing trend accompanying the low levels of misconduct and high levels of reporting—increasing whistle-blower retaliation, pressure to compromise ethical standards, and number of companies with weak ethical cultures. Forty-two percent of employees indicated that their company has a weak ethical culture, including the measures of ethical leadership, supervisor reinforcement of ethical behavior, and peer commitment. The survey notes that employees have now become less confident in their ability to handle situations dealing with ethics. New types of ethical violations are becoming prevalent—for example, environmental violations—but the largest increases in risk of misconduct occurred in the categories of sexual harassment and substance abuse. Misuse of company time, abusive behavior, abuse of company resources, lying to employees, and violating company Internet use policies were the five most frequently observed types of misconduct in 2011.

A major factor in these new trends is the influence and use of social media at the workplace. Several drivers are critical in reducing ethics risk: a well-implemented ethics program and a strong ethical culture. If U.S. businesses viewed ethics as building reputational capital—protecting corporate brand and preventing misconduct—ethics risk in the U.S. would be substantially reduced.[67] The survey reported that ethics risk is reduced when there are lower levels of misconduct, greater awareness of wrongdoing, and a reduction in retaliation of reporting.[68] Interestingly, the same survey found that only 29% of U.S. companies actually have strong ethical cultures. On a less than positive note, the survey concluded that these results were "borne out by a wave of major corporate scandals that wiped out whole companies and cost thousands of employees their jobs. Given this history, there is reason to

Figure 6.6

Contingency Alignment Model



be concerned that the current weakness of ethics cultures could foreshadow a new surge in misconduct."[69]

What is organizational culture and why is it so important to supporting ethical activities and curtailing unethical actions? According to the ERC, four elements that shape ethical culture are: (1) ethical leadership, (2) supervisor reinforcement, (3) peer commitment to ethics, and (4) embedded ethical values. Studies on culture generally show that coupled with leadership, organizational culture is central to a firm's overall effectiveness and operating efficiency. As Figure 6.6 illustrates, culture is also the "glue" that holds the other organizational dimensions (strategy, structure, people, systems) together. Strong organizational cultures are possible only with strong leaders who model, build, and help sustain legal and ethical cultures through well-defined and comprehensively implemented ethics and compliance programs.

Organizational Culture Defined

A corporation's culture is the shared values and meanings its members hold in common, which are articulated and practiced by an organization's leaders. Purpose, embodied in corporate culture, defines organizations.

Corporate culture is transmitted through: (1) the values and leadership styles that the leaders espouse and practice, (2) the heroes and heroines that the company rewards and holds up as models, (3) the rites and symbols that organizations value, and (4) the way that organizational executives and members communicate among themselves and with their stakeholders.

Heroes and heroines in corporations set the moral tone and direction by their present and past examples. They are the role models; they define what is successful and attainable; they symbolize the company to outsiders and

insiders; and they preserve the valued qualities of the firm, set standards of excellence, and motivate people. Enduring corporate and organizational cultural heroes include Warren Buffet at Berkshire Hathaway, Herb Kelleher at Southwest Airlines, Sam Walton at Wal-Mart, Ben Cohen and Jerry Greenfield at Ben & Jerry's, Mary Kay at Mary Kay, David Packard at Hewlett-Packard, and Bill Gates at Microsoft. Who are the heroes and heroines in your organization? By what qualities and characteristics are they remembered? Are they moral, immoral, or amoral leaders?

Rituals in companies help define corporate culture and its moral nature. Zappos, a retail shoe and clothing company, has an interesting, quirky and creative culture that stresses and balances family with innovation values. Their employees are close-knit and emphasize caring as well as productivity; they are also involved in community service. The company's values include: "Deliver WOW Through Service, Embrace and Drive Change, Create Fun and A Little Weirdness, Be Adventurous, Creative, and Open-Minded, Pursue Growth and Learning, Build Open and Honest Relationships With Communication, Build a Positive Team and Family Spirit, Do More With Less, Be Passionate and Determined, Be Humble."[70]

Corporately sanctioned rituals that bring people together, foster openness, and promote communication can lower stress and encourage moral behavior. Social gatherings, picnics, recognition ceremonies, and other company outings where corporate leaders are present and values, stories, problems, accomplishments, and aspirations are shared, can lead to cultures that value people and the company's aims. Does ethics matter for an organization's survival and market effectiveness? The "good management hypothesis" suggests that there is a positive relationship between a corporation's performance and how it treats its stakeholders. Studies confirm this hypothesis.[71]

Observing Organizational Culture

Organizational cultures are both visible and invisible, formal and informal. They can be studied by observation, by listening to and interacting with people in the culture, and in the following ways:

- Studying the physical setting.
- Reading what the company says about its own culture.
- Observing and testing how the company greets strangers.
- Watching how people spend time.
- Understanding career path progressions.
- Noting the length of tenure in jobs, especially for middle managers.
- Observing anecdotes and stories.

How ethically is your organizational or company culture using these methods?

Traits and Values of Strong Corporate Cultures

Strong corporate cultures (1) have a widely shared philosophy, (2) value the importance of people, (3) have heroes (presidents and products) that symbolize the success of the company, and (4) celebrate rituals, which provide

opportunities for caring and sharing, for developing a spirit of "oneness" and "we-ness."[72] From a stakeholder management view, organizational systems are aligned along the purpose, ethical values, and mission of the company. Also, individuals and teams in ethical cultures demonstrate a tolerance and respect for individual differences, compassion, ability to forgive and accept, and freedom and courage to do the right thing in questionable situations. The authors of the ERC survey referred to above state that "by every measure, strong ethics programs and strong ethics cultures produce substantially better outcomes—less pressure, less misconduct, higher reporting, and less retaliation—than in weaker ethical environments."[73] Moreover, the same survey concluded that 30% of employees observe misconduct in strong cultural environments as opposed to 89% in weaker cultures. Twenty-nine percent of employees working in companies with strong ethical cultures who reported misconduct experienced retaliation as a result, compared to the 46% who experienced retaliation in weak cultural environments.[74] As discussed below, fear and retaliation prevent reporting of illegal and unethical acts by employees.

Corporate values statements serve as the economic, political, social, and ethical compasses for employees, stakeholders, and systems. Two classic benchmark values statements are those of Johnson & Johnson (Figure 6.3) and Borg-Warner (Figure 6.4). Seattle-based Boeing Corporation's values were first articulated by its former CEO William Allen. These values still serve as an outstanding example at the individual level. They are:[75]

- Be considerate of my associates' views.
- Don't talk too much . . . let others talk.
- Don't be afraid to admit that you don't know.
- Don't get immersed in detail.
- Make contacts with other people in industry.
- Try to improve feeling around Seattle toward the company.
- Make a sincere effort to understand labor's viewpoint.
- Be definite, don't vacillate.
- Act—get things done—move forward.

High-Ethics Companies

What would a highly effective values-based organizational culture look like? Mark Pastin studied 25 "high-ethics, high-profit" firms, which at the time included Motorola, 3M, Cadbury Schweppes, Arco, Hilby Wilson, Northern Chemical, and Apple. Although the list of high-ethics firms—like "built-to-last" firms—may change, the four principles that Pastin used to describe such firms serve as a benchmark for understanding ethically effective organizations:

1. High-ethics firms are at ease interacting with diverse internal and external stakeholder groups. The ground rules of these firms make the good of these stakeholder groups part of the firm's own good.

2. High-ethics firms are obsessed with fairness. Their ground rules emphasize that the other person's interests count as much as their own.
3. In high-ethics firms, responsibility is individual rather than collective; individuals assume responsibility for the firm's actions. The ground rules mandate that individuals are responsible for themselves.
4. The high-ethics firm sees its activities as having a purpose, a way of operating that members of the firm value. And purpose ties the firm to its environment.[76]

Many of the FoEs (firms of endearment) discussed at the beginning of this chapter demonstrate these principles, for example Amazon, Costco, New Balance, IKEA, eBay, LL Bean, Wegmans, Google, Patagonia, Harley-Davidson, and REI, to name a few.

Weak Cultures

What about companies that are not ethical? Companies that reinforce secrecy, hidden agendas, and physical settings that isolate executives from managers and employees, and emphasize status over human concern, often are cultures in trouble. Troubled corporate and organizational cultures can breed and encourage unethical activities, as illustrated by Enron, WorldCom, Adelphia, Arthur Andersen, and so many other firms that have been involved in corporate scandals. Figure 6.7 shows results of the ERC's 2012 survey with regard to the observing and reporting of misconduct in strong and weak cultures.

Organizations that also overstress hypercompetition, profit at any cost, and singular economic or introverted self-interest over stakeholder obligations, and that have no moral direction, often have cultures in trouble. Signs of cultures in trouble, or weak cultures, include the following:[77]

Figure 6.7

Ethical Conduct in Strong and Weak Cultures

The Ethics Resource Center states that ethics is a component of culture. The group measured culture through three dimensions:

1. Ethical leadership / tone at the top.
2. Supervisor reinforcement of ethical behavior.
3. Peer commitment / supporting one another in doing right.

In weaker cultures misconduct is more prevalent:

- Strong cultures: 29% of employees observed misconduct the previous 12 months.
- Weak cultures: 90% of employees observed misconduct the previous 12 months.
- Strong-leaning cultures: Reported misconduct was 46%.
- Weak-leaning cultures: Reported misconduct was 67%.

Source: Ethical Resource Center (ERC). (2012). *2011 National business ethics survey,* 20. *Ethics.org.* http://www.ethics.org/nbes/files/FinalNBES-web.pdf, accessed January 10, 2010.

- An inward focus.
- A short-term focus.
- Morale and motivational problems.
- Emotional outbursts.
- Fragmentation and inconsistency (in dress, speech, physical settings, or work habits).
- Clashes among subcultures.
- Ingrown subcultures.
- Dominance of subculture values over shared company values.
- No clear values or beliefs about how to succeed in business.
- Many beliefs, with no priorities about which are important.
- Different beliefs throughout the company.
- Destructive or disruptive cultural heroes, rather than builders of common understanding about what is important.
- Disorganized or disruptive daily rituals.

In an earlier survey the ERC found that "severe" ethical risks for businesses with weak cultures included "1. Lying to employees, 2. Abusive behavior, 3. Discrimination, 4. Lying to stakeholders, 5. Misreporting hours worked, 6. Safety violations, 7. Putting own interests ahead of the organization, 8. Improper hiring practices, 9. Sexual harassment, 10. Stealing/Provision of low quality goods and services, 11. Environmental violations, 12. Internet abuse, 13. Misuse of confidential organization information, and 14. Alteration of financial records."[78]

One of the worst corporate cultures in recent history was Enron's. Malcolm S. Salter, Harvard Business School professor, described Enron's culture the following way:

> Enron is a case about how a team of executives, led by Ken Lay, created an extreme performance-oriented culture that both institutionalized and tolerated deviant behavior. It's a story about a group of executives who created a world that they could not understand and therefore could not control. It's a story about the delinquent society—and I use that phrase intentionally—that grew up around the company, and here I'm referring to the collusion of Enron's various advisors and financial intermediaries. And most importantly, Enron is a story about how fraud is often preceded by gross incompetence: where the primary source of that incompetence is inexperience, naiveté, an ends-justify-the-means attitude toward life, and so on. And most importantly, an inability to face reality when painful problems arise.[79]

A values-based stakeholder management approach would assess an organization's values with these questions: Do the leaders and culture embody "high-ethic" or "in trouble" characteristics in their values, actions, and policies? Are the values written down? Do others know the values? Do the values reflect a concern for and obligation toward the organization's stakeholders? Do the values reflect a utilitarian, just, dutiful, or egotistical ethic? Are the

values taken at "face value" only, or are they practiced and implemented by employees? Do the values and communication patterns promote moral, immoral, or amoral behavior?

6.3 Leading and Managing Strategy and Structure

If culture is the glue that holds organizations together, strategy maps the direction. The moral dimensions of strategy are also based on ethics. People are motivated to implement strategies that they believe in, are able to enact, and that produce results. Strategy and the strategy development process are the domain of organizational leaders. Gary Hamel, a contemporary strategy guru, calls for a "revolution" in leading the strategy innovation process. He states that "you need a set of values that will set you apart from the courtiers and wannabes." Those values include "honesty, compassion, humility, pragmatism, and fearlessness."[80] The strategy-making process also involves stakeholder management. A corporation's strategy is propelled and supported by its people, stakeholders, culture, and moral contributions to its communities, customers, and society. Strategic thinking has evolved from a mechanistic process to a more holistic process, which emphasizes innovation, generation of value for stakeholders and stockholders, involvement and learning with stakeholders, and building customer partnerships and relationships.[81] This section and the next discuss the relationships between corporate strategy, structure, culture, systems, and moral responsibility. How do strategy and structure influence the moral behavior of employees?

Corporate leaders are responsible for orchestrating the development and execution of strategy. An organization's strategy influences legality, morality, innovation, and competitiveness in the following ways:

1. Strategy sets the overall direction of business activities. Enterprise strategy, for example, can emphasize revenue and growth over customer satisfaction or product quality. It can drive technical concern over professional development. Corporate strategy can also direct a firm's activities toward social issues, employee rights, and other stakeholder obligations. It can include or exclude stakeholders and employees. It can innovate recklessly for the short term or in long-term ways that benefit society as well as a few market niches.

2. Strategy reflects what management values and prioritizes. It mirrors management's ethics and morality. It is the message to the messengers. Strategy says: "We care and value your feedback, safety, and concerns," or "We only want your money and participation in our profits."

3. Strategy sets the tone of business transactions inside the organization. Reward and control systems reflect the values of the larger strategic direction. An emphasis on profit at the expense of employee development is usually reflected as rigid and unrealistic incentive and revenue quota systems. Growth and expansion can be made a priority at the expense of talent development and contribution.

Marianne Broadbent, a leading scholar in information technology, offers the following insights about strategy:

> When creating a strategy, I see a number of steps: the aspiration, the big business principles or maxims, then having a number of scenarios or options which are based on a set of strategic assumptions that you constantly, constantly pick to see if they are in sync. And then you use that information to shift and change. At a tactical level, that means rolling out products and services in a very careful, risk-managed way so that you can sense and respond to the marketplace.
>
> Strategy is very much about synchronizing the enterprise with its external environment as much as possible. Think about how increasingly interconnected economies, markets, technology and political situations are. September 11 is a great example of how quickly things can change and how interdependent logistics, for example, is with strategy, with customer service, with the politics of what's going on at the moment. I look at strategy more as synchronization, and that which focuses much more on what we call the market inputs rather than the outputs.[82]

From a values-based stakeholder management approach, the strategy development and implementation process should reflect the vision and mission of the organization. As with the Levi Strauss's values and vision statement in Figure 6.2, the strategy would be reviewed from these statements: "Integrity—Doing the Right Thing. Ethical conduct and social responsibility characterize our way of doing business. We are honest and trustworthy. We do what we say we are going to do. Integrity includes a willingness to do the right thing for our employees, brands, the company and society as a whole, even when personal, professional and social risks or economic pressures confront us. This principle of responsible commercial success is embedded in the company's experience. It continues to anchor our beliefs and behaviors today and is one of the reasons consumers trust our brands. Our shareholders expect us to manage the company this way. It strengthens brand equity and drives sustained, profitable growth and superior return on investment. In fact, our experience has shown that our 'profits through principles' approach to business is a point of competitive advantage."

A firm should identify issues that affect its stakeholder obligations and relationships while developing strategies. From a social and moral perspective, managers should be concerned about fulfilling their internal stakeholder obligations through these strategies. Responsible corporations must be prepared to equitably and justly enable the workforce with new technical skills and integrate aging employees, dual-career families, and new immigrants. Flexible work times, health care programs, and flexible management styles must be implemented to manage this changing workforce responsibly.

Organizational Structure and Ethics

Structure is another organizational dimension, shown in Figure 6.6, along with strategy and culture, that is part of an organization's infrastructural makeup. Ask to see almost any organization's structure and you will be

handed a hierarchical set of boxes connected by lines. This so-called pyramid, or functional structure, is one of the oldest forms of depicting arrangements in companies.

Regardless of the specific type of structure, from an ethical, values-based stakeholder management perspective, key concerns and questions regarding any structure are:

- How centralized or decentralized are the authority, responsibility, communication, and information flow?
- How organic (less structured) or mechanistic (more structured) are the systems?
- How tall (more layers of bureaucracy) or flat are the reporting systems?
- How formal or informal are procedures, rules, and regulations?
- How much autonomy, freedom, and discretion do internal stakeholders and decision makers have?
- How flexible, adaptable, and responsive are systems and professionals to responding to internal and external threats, opportunities, and potential crises?

Although there are no absolute guidelines regarding which structure is more immune to or leads to ethical problems, the following overview provides some evidence about how structure relates to ethical behavior. Functionally *centralized* structures can encourage lack of communication, coordination, and increased conflict because each area is typically separated by its own boundaries, managers, and systems. Infighting over budgets, "turf," and power increase the likelihood of unethical, and even illegal, activities. For example, post-September 11, 2001, reports show the overly centralized CIA and FBI communicated poorly with each other, with the White House, and with other systems of government.

On the other hand, highly supervised employees in bureaucratic firms may also act more ethically than employees in entrepreneurial, laissez-faire firms because employees tend to think through the risk of getting caught in firms with more supervised structures. A study conducted by Cullen, Victor, and Stephens reported that a subunit's location in the organizational structure affects its ethical climate.[83] At a savings and loan association and also at a manufacturing plant, the employees at the home offices reported less emphasis on laws, codes, and rules than did the employees at the branch offices. Perhaps control by formal mechanisms becomes more necessary when direct supervision by top management is not feasible.

There is evidence that *decentralized* structures can encourage more unethical behavior among employees than more supervised, controlled structures. Citicorp's credit card processing division illustrated the relationships among organizational structure, competitive pressures, and immoral and illegal behavior. The bank fired the president and 11 senior executives of that division because they fraudulently overstated revenue by $23 million for two years. The inflating of revenue by division employees may have been related to the fact that employee bonuses were tied to unrealistic revenue targets. Citicorp

centralized its organizational functions. In this case, the decentralized structure left the bank susceptible to potential abuse by employees. On the other hand, some decentralized structures may enable individually responsible and ethical professionals to communicate their beliefs and report errors faster, up and down a more fluid chain of command.

Pressures from upper-level managers who overemphasize unrealistic quarterly revenue objectives and who give unclear policies and procedures to guide ethical decision making may also contribute to immoral behavior in more decentralized structures. There is evidence to support the argument that middle- and lower-level managers, in particular, feel pressured to compromise their personal moral standards to meet corporate expectations.[84] Managers in large firms may compromise their personal ethics to meet corporate expectations for several reasons, which include:

1. Decentralized structures with little or no coordination and central policy and procedures encourage a climate for immoral activities when pressures for profit making increase.
2. Unrealistic short-term and bottom-line profit quotas add pressure on employees to commit unethical actions.
3. Overemphasis on numbers-driven financial incentives encourages shortcuts.
4. Amoral organizational and work-unit cultures can create an environment that condones illegal and immoral actions.

Boundaryless and Networked Organizations

The decentralization of organizations has been accelerated by information technology and the reengineering of business processes. Software applications and Web-enabled intranets and extranets allow the boundaries within organizations and between customers and companies to become more transparent and fluid.[85] Dell Computer has eliminated middle layers of its company, supply chain, and industry by enabling individual customers to design, order, and purchase—and even receive, in the case of software—their own customized computer products online. These changes are not easy, nor are they isolated from the larger context of the organization. An organizational expert noted that the main reason implementation of major technology changes fails is that "the technology was seen as the solution, without taking into account the complex dynamic of the organization and people. It doesn't matter in which area, whether it's knowledge management or B2B. You can't forget that organizations are made of people and technology, and both people and technology will define the success of an organization."[86]

From both an ethics and efficiency perspective, care should be taken by companies implementing digital networks, because one study has reported that digital networks generate both opportunities for and threats to worker autonomy.[87] Major opportunities include increased communication capabilities, "informedness," and "teleworking." Threats to worker autonomy are electronic monitoring, dependence on third-party operators and managers,

and task prestructuring, which can reduce individual responsibility and control. These opportunities and problems depend, in part, on the type of organizational structure in place: how open and responsive it is or how closed and vulnerable it may be to unethical activities.

6.4 Leading Internal Stakeholder Values in the Organization

The other internal dimensions of organizations, illustrated in Figure 6.6, should also be aligned in order for the organization to succeed in meeting its goals and social responsibility obligations. In practice, aligning an organization's values and mission with its internal stakeholders, while treating external groups and organizations ethically, is difficult because of competing values of internal stakeholders. The following quote from Anderson illustrates the diversity among stakeholder values:

> An organization in almost all its phases is a reflection of competing value choices. Owners want a return on their investment. Employees want secure jobs and career development. Managers want growth and industry leadership. Government regulators want minimal pollution, safety, work opportunities for a wide variety of groups, and tax revenues. For top managers, this competition comes to a head because they must unravel complex problems whose solutions benefit some groups but have negative consequences for others. Framing these decisions inevitably leads to some crucial dilemmas for managers, who must answer the broad question, "What is a convincing balance among competing value choices?"[88]

R. Edward Freeman and Daniel Gilbert Jr. argued that we must understand the multiple and competing values underlying stakeholders' actions in order to understand the choices corporations make.[89] Balancing internal stakeholder interests can be difficult because of the diversity of professional and functional backgrounds, training, goals, time horizons, and reward systems. These differences are further influenced by organizational politics, the constraints and pressures of other internal systems, and changing roles and assignments. Figure 6.8 is an example of an organization's internal stakeholders and competing professional value orientations.

Function orientations, such as marketing, research and development (R&D), production, information systems, and finance, have built-in competing values, especially when employees who are under pressure must design, deliver, and service complex products and services for demanding customers. Marketing and sales professionals work with short- to medium-term time horizons and are rewarded on the basis of their results. Sales professionals, in particular, have a very short time horizon and depend on the success of individual and team selling abilities to satisfy, retain, and attract customers. R&D professionals generally have a longer time horizon and are rewarded for their innovations.

Figure 6.8

A Functional Profile of Internal Organizational Stakeholders: Professional Orientations

Professional Stakeholders					
Orientations	**Marketing and Sales**	**Research and Development (R&D)**	**Production**	**Finance and Accounting**	**Information Systems**
Background	Liberal arts; social sciences; entrepreneurial; technical	Electrical engineering; technical	Mechanical engineering; operations	Finance; accounting; auditing; tax	Software "engineers"; data management; programming
Goals and "Stakes"	High product mix; revenue and market competitiveness; customer satisfaction	Market dominance; innovation; competitiveness	Product yield; Quality control	Low-cost capital; efficient borrowing; accountability	Problem solving; organizational integration; systems functioning
Focus and Rewards	Product or service leadership; creative autonomy; bonuses; equity; career mobility	Next "killer" application; resources to innovate; prestige	Product Lifecycle stability; peace with R&D job security; bonuses	Low costs; high yields; data access; accuracy; cooperation; career advancement	Satisfied users; state-of-the-art technology; career advancement; new skill development
Time Horizon	Short to medium time frame	Medium to long time frame	Short to continuous time frame	Continuous time frame	Continuous time frame

The contrast between marketing and sales professionals and R&D professionals is shown in Figure 6.8, and you can see how value differences and role conflicts can occur within cross-functional teams. Competition and conflict can lead to higher productivity and also to unethical decisions and practices, such as producing unsafe products or lying to customers to make a sale.

From a stakeholder management perspective, it is the role of an organization's leaders, with the support of each professional, to ensure that the internal integrity and market effectiveness of a company is based on the types of relationships and values that embody trust, collaboration, and a "win–win" goal for stakeholders and stockholders. Amorally and unethically led and managed organizations with conflicting internal values can, and sometimes do, lead to illegal situations. Interpersonal communication skills, conflict resolution, and collaborative negotiation methods (as exemplified in Chapter 3) are also needed to help integrate these functional area differences.

Value and innovation are created when the collaborative efforts of an organization's systems create synergy. The organization's vision, values, and mission, which are reinforced by the culture and example of the leaders, are the cornerstone for integrating structures and systems. Following this logic,

Kim and Mauborgne posed the following research question: "What type of organization best unlocks the ideas and creativity of its employees to achieve this end?"[90] They discovered that "when putting value innovation strategies into action, structural conditions create only the potential for individuals to share their best ideas and knowledge. To actualize this potential, a company must cultivate a corporate culture conducive to willing collaboration."[91]

These authors see "the positively reinforcing cycle of fair process" as one which creates innovative outcomes for companies. They describe this process as follows: For each success a group has in implementing a "general value innovation strategy" based on fair process, the result strengthens the group's cohesiveness and their belief in the process. This, in turn, sustains the collaboration and creativity inherent to value innovation. The four components of that process include:[92]

1. Engagement, explanation, expectation, clarity.
2. Idea sharing and voluntary cooperation.
3. Value innovation plans and rapid execution.
4. Organizational confidence in and respect for colleagues' intellectual and emotional worth.

6.5 Corporate Self-Regulation and Ethics Programs: Challenges and Issues

According to the ethicist Lynn Paine in a *Harvard Business Review* article, a values-based approach in ethics programs should be more effective than a strict, rules-based compliance approach, since a values approach is grounded and motivated in personal self-governance.[93] Employees are more likely to be motivated to "do the right thing" than threatened if they violate laws and rules. A values-based stakeholder management approach assumes that corporations (owners and management) ought to intrinsically value the interests of all stakeholders.[94] In practice, this is not always the case.[95] Later studies suggest that both values-based and compliance ethics programs seem to work effectively together. Without values-based compliance, however, compliance and fear-based programs are less likely to succeed.[96] Responsible self-regulation in companies can enhance entrepreneurship and reduce unnecessary costs of too much bureaucratic control (e.g., it is estimated that the 2002 Sarbanes-Oxley Act costs large public companies $16 million to implement). One study by the Open Compliance Ethics Group (OCEG) found that firms that had had an ethics program for 10 or more years did not have "reputational damage" during the last five years. Ethics programs appear to have some intended effect.[97] Complete your company's "Ethical Weather Report" to identify your point of view regarding how ethical your company is.

Chapter 4 discussed in more detail ethics programs that include codes of ethical and legal conduct that are designed to help companies financially and legally. As noted there, the Federal Sentencing Guidelines for Organizations (FSGO) were established in 1984 by Congress—which passed a crime bill

that instituted the U.S. Sentencing Commission. This commission, made up of federal judges, was empowered with sentencing those found in violation of the guidelines. In 1987, uniform guidelines were created for sentencing individuals in the federal courts. Some federal judges quit the bench in protest of the strictness of the guidelines and the sentences they were required to hand down. In 1991, the commission shifted the emphasis from individual wrongdoers to organizations that might be found guilty for the illegal actions of their employees. The 1991 revised guidelines threaten fines of up to $290 million to companies found guilty of violating the federal guidelines. However, those fines can be substantially reduced if an organization implements an "effective program to prevent and detect violations of law." Companies that followed the requirements of the FSGO could find relief from lawsuits that resulted from one or more criminally motivated professionals. However, without active, ethical leadership, there is less likely to be a strong culture, open communication, and support from other organizational systems to support ethics programs.

Ethical Insight 6.3

Ethical Climate of Your Organization

Step 1: Complete the following questionnaire using the organization employing you now or in the recent past. Record the number beside each item from the scale that realistically reflects your experience with and understanding of the organization.

0 = Completely False, 1 = Mostly False, 2 = Somewhat False, 3 = Somewhat True, 4 = Mostly True, 5 = Completely True

_____ 1. In this organization, people can, and often do, follow their own principles and belief systems.
_____ 2. Employees and professionals are expected to do what it takes to achieve the organization's goals and interests.
_____ 3. Individuals and groups generally protect and advance each other's interests.
_____ 4. Dutifully following the organization's rules and decisions are strongly expected.
_____ 5. Everyone protects themselves over others' interests in this organization.
_____ 6. The law, rules, and regulations are first and foremost with authority here.
_____ 7. People are strictly expected to stay within the organization's authoritative rules.
_____ 8. Efficiency is oftentimes more important than effectiveness in this organization.
_____ 9. People are considerate to and for others in this organization.

_____ 10. Professional ethical codes and principles are very important in this organization.
_____ 11. People in this organization are rewarded for promoting the interests of customers and stakeholders.

Step 2: Add your responses to 1, 3, 6, 9, 10, and 11. Write the sum after "Subtotal 1" below. Now reverse the scores on questions 2, 4, 5, 7, and 8 (5 = 0, 4 = 1, 3 = 2, 2 = 3, 1 = 4, 0 = 5). Add these reverse scores (i.e., number value) and write the sum after "Subtotal 2" below. Now add Subtotal 1 with Subtotal 2 for your overall score. The total score ranges between 0 and 55. The higher the score, the more the organization supports ethical behavior.

Subtotal 1 _____ + Subtotal 2 _____ = Overall Score _____

Step 3: Write a statement describing your organization's ethics. Explain why the organization is as you describe it. How does/did the ethical climate affect you, your attitudes, energy, motivation, and ethical orientation?

Step 4: What would you say to the leaders and staff of this organization, if you could, regarding the culture, policies, procedures, and ethical environment? What recommendations would you offer to change the climate and culture of the organization?

Source: Reprinted from Cullen, J. B., Victor, B., and Stephens, C. (Autumn 1989). An ethical weather report: Assessing the organization's ethical climate. *Organizational Dynamics, 18,* 50–62, with permission from Elsevier.

Organizations and Leaders as Moral Agents

Since corporations are charted as citizens of states and nations, they also share the same rights and obligations as citizens. Corporations are not, however, individuals; they are moral agents that must follow laws, rules, and regulations of their local and national settings. When corporations violate such laws, they are also subject to penalties and fines, and can even have their right to exist taken away, depending on judicial findings in criminal acts (as was the case with Arthur Andersen). The role of leaders as moral agents has not been emphasized enough as one of the key ingredients in building and sustaining ethics programs. Organizational leaders who lack strong moral character and convictions, even if they are brilliant strategists and execute excellently, leave their firms vulnerable to illegal and unethical acts, as Enron clearly showed.

Ethics Codes

Ethics codes are value statements that define an organization. Leaders' values again play a significant role in shaping the values of the organizations in which they serve. Six core values that researchers have found desirable in such codes include (1) trustworthiness, (2) respect, (3) responsibility, (4) fairness, (5) caring and (6) citizenship.[98] Johnson & Johnson's Credo (Figure 6.3) is

an outstanding example. Raytheon, Fidelity, Honda, and other firms in the FoE list in this chapter have ethics and codes of conduct that are noteworthy. Major purposes of ethics codes include:[99]

- To state corporate leaders' dominant values and beliefs, which are the foundation of the corporate culture.
- To define the moral identity of the company inside and outside the firm.
- To set the moral tone of the work environment.
- To provide a more stable, permanent set of guidelines for right and wrong actions.
- To control erratic and autocratic power or whims of employees.
- To serve business interests (because unethical practices invite outside government, law enforcement, and media intervention).
- To provide an instructional and motivational basis for training employees regarding ethical guidelines and for integrating ethics into operational policies, procedures, and problems.
- To constitute a legitimate source of support for professionals who face improper demands on their skills or well-being.
- To offer a basis for adjudicating disputes among professionals inside the firm and between those inside and outside the firm.
- To provide an added means of socializing professionals, not only in specialized knowledge, but also in beliefs and practices the company values or rejects.

Codes of Conduct

An organization's code of conduct is only as credible as the CEO's and leaders' personal and professional codes of conduct. Leaders must "walk the walk" as well as "talk the talk." "An organization's code of conduct, alternatively referred to as 'code of ethics' or 'code of business standards,' is the stated commitment of the behavioral expectations that an organization holds for its employees and agents. Such codes are now commonplace for most corporations and are increasingly shared not only with employees, but also with customers and the public at large. To be successful, a code must be believable by all stakeholders to which it applies. A corporation's leaders must show commitment to communication and fairly enforcing codes of conduct for such documents to be effective. However, how the code is written and what it contains are also important elements regarding whether it has the power to influence not only perceptions, but actions."[100]

One survey of U.S. corporate ethics codes found that the most important topics were general statements about ethics and philosophy; conflicts of interest; compliance with applicable laws; political contributions; payments to government officials or political parties; inside information; gifts, favors, and entertainment; false entries in books and records; and customer and supplier relations.[101] Notable firms go further in detailing corporate obligations. The examples of Johnson & Johnson and BorgWarner (Figures 6.3

and 6.4) define their obligations to various stakeholders. Other exemplary codes include those of General Electric, KMPG, PricewaterhouseCoopers, Boeing, General Mills, GTE, Hewlett-Packard, McDonnell Douglas, Xerox, Norton, Chemical Bank, Champion International, Mattel, Hershey's, Ford Motor Company, the Coca-Cola Company, American Express, UPS, and IKEA.

Examples of items in a code of conduct include the following list:[102]

- Financial Integrity & Assurance
- Ethical Principles
- Intellectual Property
- Information Security
- Workplace Violence
- Insider Trading
- Illegal Business Practices
- OSHA (Occupational Safety and Health Administration) guidelines
- Legal & Effective E-mail
- Anti-Money Laundering
- Conflicts of Interest
- Health & Safety
- Harassment
- Record Keeping & Destruction
- Gifts & Gratuities
- Antitrust
- Diversity

Companies looking to buy (acquirers) other companies (targets) perform preacquisition due diligence on the management, finance, technology, services and products, legality, and ethics of the targets. That is, companies looking to purchase other companies need to perform analyses to discover if the targets are telling the truth about their products, finances, and legal records. "Where does one start in uncovering the ethical vulnerability of a target?" The following basic questions are suggested as a starting point:[103]

1. Does the target have a written code of conduct or code of ethics?
2. Does the company provide ethics training or ethics awareness-building programs for management and company employees?
3. Are avenues, such as an ethics office or hotline, available for employees to ask questions about ethical issues?

Problems with Ethics and Conduct Codes

The problems with corporate ethics codes in general are the following:[104]

1. Most codes are too vague to be meaningful; that is, the codes do not inform employees about how to prioritize conflicting interests of distributors, customers, and the company. What does being a "good citizen" really mean in practice?
2. Codes do not prioritize beliefs, values, and norms. Should profit always supersede concern for customers or employees?
3. Codes are not enforced in firms.
4. Not all employees are informed of codes.
5. Codes do not relate to employee's actual work and ethical "gray" areas.

6. Top-level leaders in organizations usually do not show interest or involvement in the programs.
7. Codes do not inspire or motivate employees to follow law, rules, and procedures.
8. Codes that are used internationally have sections that are irrelevant or incomplete to other country personnel's experiences and specific areas of concern.

Ethics codes are a necessary but insufficient means of assisting or influencing professionals with managing moral conduct in companies. One study showed that companies that had corporate ethics codes had "less wrongdoing and higher levels of employee commitment."[105] However, the authors explain that "formal ethical codes are one component of a milieu that encourages and supports high standards of ethical behavior; that is, these organizations have formal and informal mechanisms to ensure that ethical conduct becomes 'a way of life.'" Also, employee behavior was not as influenced by the ethics codes because the codes "are not part of the organizational environment." Part of the message here may also be that implementing several organizationally supported and integrated values-based stakeholder management and ethics programs has a better chance of meeting intended goals than does reliance on brochures and printed documents.

Ombuds and Peer-Review Programs

Ombuds and peer review programs are additional methods that corporations use to manage the legal and moral aspects of potentially problematic activities in the workplace. The ombuds approach provides employees with a means of having their grievances heard, reviewed, and resolved. Originating in Sweden, this concept was first tried at Xerox in 1972 and later at General Electric and Boeing. Ombuds individuals are third parties inside the corporation to whom employees can take their grievances. At Xerox, employees are encouraged to solve their problems through the chain of command before seeking out the ombudsperson. However, if that process fails, the employee can go to the ombudsperson, who acts as an intermediary. The ombuds individuals, with the employee's approval, can go to the employee's manager to discuss the grievance. The ombudsperson can continue through the chain of command, all the way to the president of the corporation, if the problem has not been satisfactorily resolved for the employee. Ombudspersons have no power themselves to solve disputes or override managers' decisions. Complaints usually center on salary disputes, job performance appraisals, layoffs, benefits, and job mobility. At General Electric, ombudspersons report that they handle 150 cases every year.

The International Ombudsman Program recently stated on its web site, "The legislative and corporate governance environment has changed in recent years. It is more critical than ever for companies to have a complete system for identifying and resolving ethics problems. Such a system works best if it combines formal channels such as hotlines and compliance policies with the

informal channel of an ombuds office, which remains independent of the company's management structure."[106]

An example of an effective ombuds program is that of the International Franchise Association (IFA). Its board of directors adopted a comprehensive self-regulation program that has a clearly and strongly stated ethics code; an investor awareness and education program; a franchise education compliance and training program; a code enforcement mechanism; and an ombudsperson program, which is described as follows: "The ombudsperson program is designed to enable franchisors and franchisees to identify disputes early and to assist them in taking preventative measures . . . facilitating dispute resolution . . . recommending non-legal methods and approaches to resolving disputes, encouraging [both parties] to work together to resolve disputes, providing confidentiality throughout the process, and providing objective and unbiased advice and guidance to all the participants."[107]

A problem with the ombuds approach is that managers may feel their authority is threatened. Employees who seek out ombudspersons also might worry about their managers retaliating against them from fear or spite. Confidentiality also has to be observed on the part of ombudspersons. The ombudsperson is as effective as the support of the program by stakeholders allows him or her to be. An ombudsperson's success is measured by the trust, confidence, and confidentiality he or she can create and sustain with the stakeholders. Finally, the ombudsperson's effectiveness depends on the acceptance by managers and employees of the solutions adopted to resolve problems. Ombuds programs, for example, have been successful at IBM, Xerox, General Electric, the U.S. Department of Education, Boeing, The World Bank, and several major U.S. newspaper organizations.

Peer review programs have been used by more than 100 large companies to enable employees to express and solve grievances, thus relieving stress that could lead to immoral activities. Employees initially use the chain of command whenever a problem exists. If the supervisors or executives do not resolve the problem, the employee can request a peer review panel to help find a solution. Two randomly selected workers in the same job classification are chosen for the panel along with an executive from another work unit. The selection must be reviewed in reference to company policy. Peer review programs work when top management supports such due process procedures and when these mechanisms are perceived as long-term, permanent programs.

Peer review programs have received positive reviews and have had good results, particularly in the health care and accounting industries. More than 50% of the U.S. state boards of accountancy require certified public accountants to participate in a peer review program to obtain a license to practice.[108] Congress has mandated the use of the Medicare Peer Review Organization since 1982.[109] In England, peer review accreditation programs have evolved as external voluntary mechanisms that also provide organizational development of health care providers.[110] Ombudsperson and peer review programs serve as popular mechanisms not only for solving disputes among stakeholders, but also for integrating the interests of diverse stakeholders.

We conclude this chapter by presenting a "Readiness Checklist" organizations can use to determine whether or not their executives and professionals use a values-based stakeholder management approach to create and sustain integrity in the organization. If not, they may review their vision, mission, values statements as well as their ethics and codes of conduct. You may consider applying the checklist to your organization or institution.

Is the Organization Ready to Implement a Values-Based Stakeholder Approach? A Readiness Checklist

A values-based stakeholder readiness checklist can inform and educate (even interest and mobilize) top-level leaders to evaluate the ethics of their business practices and relationships. The following readiness checklist is an example that can be modified and used as a preliminary questionnaire for this purpose:

1. Do the top leaders believe that key stakeholder and stockholder relationship building is important to the company's financial and bottom-line success?
2. What percentage of the CEO's activities is spent in building new and sustaining existing relationships with key stakeholders?
3. Can employees identify the organization's key stakeholders?
4. What percentage of employee activities is spent in building productive stakeholder relationships?
5. Do the organization's vision, mission, and value statements identify stakeholder collaboration and service? If so, do leaders and employees "walk the talk" of these statements?
6. Does the corporate culture value and support participation and open and shared decision making and collaboration across structures and functions?
7. Does the corporate culture treat its employees fairly, openly, and with trust and respect? Are policies employee-friendly? Are training programs on diversity, ethics, and professional development available and used by employees?
8. Is there collaboration and open communication across the organization? Are openness, collaboration, and innovation rewarded?
9. Is there a defined process for employees to report complaints and illegal or unethical company practices without risking their jobs or facing retribution?
10. Does the strategy of the company encourage or discourage stakeholder respect and fair treatment? Is the strategy oriented toward the long or short term?
11. Does the structure of the company facilitate or hinder information sharing and shared problem solving?
12. Are the systems aligned along a common purpose or are they separate and isolated?
13. Do senior managers and employees know what customers want, and does the organization meet customer needs and expectations?

If answers to these questions are mostly affirmative, the internal organization most likely reflects ethical leadership, culture, and practices. If responses are mostly negative, legal and ethical problems may be imminent.

Chapter Summary

Corporate and organizational leaders set the vision, mission, and values of their enterprises. Leaders also help define the culture of companies that determine their firms' ethical and legal boundaries and contributions. A stakeholder management, values-based approach is central to organizing and aligning internal systems to respond to all stakeholders. There are still many lessons to be found in the classic "built-to-last" and "good to great" companies, whose fundamental purposes and core values were the foundation for competitive long-term achievement. More recently, highly successful companies referred to as "firms of endearment" exemplify even more of a values-based, stakeholder approach in dealing with customers, employees, suppliers, vendors, and society. This chapter offered numerous examples and evidence of effective values and stakeholder management approaches leaders use in the marketplace.

Leaders define and model the moral character of organizations. Leaders guide the identification of a vision, mission, and values and then serve as ethical role models in their stakeholder and business relationships. Figure 6.1 illustrates a strategic alignment model that leaders can use to guide their strategy development process. James Collins's "Level 5" leader profile was used as an example of successful leaders. A values-based stakeholder management approach was summarized and argued that organizations can be economically successful by being socially responsible and ethical with their stakeholders.

Leadership in organizations can be defined from a values-based approach: Leaders define and model the social and ethical as well as the competitive mission of companies. They build and sustain relationships with stakeholders while demonstrating collaboration and trust. Stakeholder management is the basis for strategic alliances. Former president of Southwest Airlines Herb Kelleher, Aaron Feuerstein of Malden Mills, and Jeffrey Swartz of the Timberland Company are a few examples of successful competitive industry leaders who lead ethically and spiritually.

Failure of ethical leadership is evidenced by seven symptoms: ethical blindness, muteness, incoherence, paralysis, hypocrisy, schizophrenia, and complacency. Mickey Monus, former CEO of the Phar-Mor company, failed to lead ethically and was sentenced to 20 years in prison for mail fraud, wire fraud, bank fraud, and theft. "Chainsaw Al" Dunlap, former CEO of Sunbeam, was fired after the SEC found fraudulent activities during his tenure.

The reasonableness of CEO pay and performance was discussed. Not all CEOs are overpaid, but there is a significant number of highly visible CEOs whose high compensation appears unrelated to their firm's performance. This remains a concern of activist shareholders.

Figure 6.6 summarizes an alignment contingency model for understanding the "big picture" of leaders' tasks in defining and implementing effective and ethical strategies, cultures, and structures. Strategies, cultures, structures, and systems are aligned along a vision, mission, and core values. This approach is compatible with the "firms of endearment," "built-to-last," and "good to great" studies of successful organizations. Customers as key stakeholders are central to an organization's alignment since they are essential to a firm's success.

Strategy must be aligned with markets, values, culture, leadership style, and structure to be effective. Strategy serves both a revolutionary role (to be innovatively competitive) and a more classical role at four levels: enterprise, corporate, business, and function. Strategies influence ethics by the expectations, pressures, motivation, and rewards they create. Overly aggressive strategies, which may also be unrealistic, can create implementation pressures that lead to unethical activities.

Culture, structure, and other systems are internal dimensions that enable leaders and professionals to implement strategy. "High-ethics" company cultures can serve as a benchmark for other organizations' cultures. Such cultures are grounded in well-defined purposes that drive operations. These cultures are also modeled by leaders who are devoted to fairness, interaction with all stakeholders, concern for stakeholder interests, and individual responsibility.

Organizational structures that are overly centralized or decentralized may foster ethical problems. Although there is not "one best way" to structure a company, there are advantages and disadvantages to each type of structure. For example, centralized functional structures discourage open communication and sharing and must be integrated. Decentralized structures, such as networks and project teams with little or no coordination, may create a climate for unethical activities, such as fraud, theft, and unfair pressure of customers and alliance partners. Having leaders who rely on mission-driven ethical values that are communicated, reflected in the culture, and enforced throughout a firm is a necessary part of structural alignment.

Figure 6.8 illustrates the challenge of balancing internal organizational and professional stakeholders' values. Professional stakeholders in marketing, R&D, sales, finance, and production often function within four boundaries: rewards, time horizons, training backgrounds, and resource constraints. A critical task of organizational leaders is to guide internal professionals and focus them on the mission and values of the company.

An overview of self-regulated ethics programs was presented. Ethics programs, codes, ombudspersons, peer reviews, and ethics officers programs are ways in which corporations can attempt to regulate themselves. Johnson & Johnson's "Credo" (Figure 6.3) is an example of an outstanding ethics code.

A "Readiness Checklist" for assessing a values-based, stakeholder readiness perspective was offered that enables firms to address the extent to which they use a values-based stakeholder approach in their business practices.

Questions

1. Describe the most ethical leader for whom you have worked. Now describe the least ethical leader. Which leader did you learn valuable lessons from and enjoy working with the most? The least? Why? What role did ethics play in your answers? Explain.
2. Describe an experience you have had (or an experience where you observed a leader) that required moral courage to either make a tough decision or refrain from making a decision that could have had harmful consequences. After describing the experience, answer these questions: (a) What was "moral" about the decision that had to be made? (b) What differentiated this situation and decision from other decisions that were serious but that did not require "moral courage"? Explain.
3. Do you believe leaders in large Fortune 500 companies follow and model their stated visions, missions, and values in everyday business dealings? Explain. Identify a Fortune 500 company and CEO in the news that demonstrates ethical behavior. Is there any evidence that his or her company's performance is related to ethical leadership behavior? Explain.
4. Do companies have to operate ethically to be financially successful? Explain.
5. Identify some characteristics of a values-based stakeholder approach to leading and running a company. Do you agree or disagree with these characteristics? Explain.
6. Which of the 13 values-based readiness checklist steps would you expect are least practiced in most companies? Which steps on the list do you believe the organization for which you work(ed) practiced least? Why?
7. Do you believe most CEOs in U.S. companies are overpaid and underperform? Explain. What pay or performance criteria do you believe should be used for top-level officers in publicly traded companies?
8. Offer one difference a values-based, ethical stakeholder approach could make in the formulation and implementation of an organization's strategy. Explain.
9. Suggest three differences a values-based, ethical stakeholder perspective could make in forming and building a new organizational culture. Explain.
10. What clues would you look for in identifying ethical and unethical activities by evaluating an organization's structure? Explain.
11. If you were to evaluate the alignment of an organization's strategy, structure, and culture from a values-based stakeholder approach, suggest three criteria you would use and some questions you would ask.
12. Which is most effective for organizational stakeholders: internal self-regulation or government regulation? Defend your points.
13. Explain the strengths and weaknesses of organizational (a) ethics codes, (b) ombuds and peer review programs, and (c) ethics departments.

Exercises

1. Assume you are an ombudsperson or an ethics officer for a large organization. What problems do you believe you would experience? Why? What contributions do you think you could make in this role? Why?
2. Describe the type of training you would need and list specific competencies that would help you in the role of ombuds or ethics officer.
3. Draft a brief values statement (or list some major values) of the ideal company for which you would like to work. Compare your list with other students' lists. What similarities and differences did you find? Compare your list to the examples in this chapter. What are the similarities or differences?
4. Briefly describe the leader of an organization in which you work or have worked. Evaluate the moral, amoral, or immoral characteristics of the leader. Refer to the "ethics of leadership styles" and the "seven symptoms of the failure–or success–of leadership" in the chapter.
5. Return to question 4. Suggest specific ways that your leader could improve his or her leadership competency and ethical style.
6. Briefly describe the culture of an organization in which you work or have worked. Explain how the culture affected a specific business practice. How ethical or unethical were the effects of the culture on that business practice? Explain.
7. Return to question 6. Suggest a few ways in which that organization's culture could be strengthened or changed. Offer a suggestion for the way the strategy formulation or implementation could be changed. Offer a way in which one of the practices or management methods of the system could be changed for improvement.

Real-Time Ethical Dilemma

Values and Leadership at Z Insurance Corp.

"What Would You Do?" I graduated from the University of New England on a beautiful day in May. Graduating cum laude, with a job in my back pocket, I thought that my future was as bright as the sun was that day. However, unlike that beautiful day, blue skies did not lie ahead for me professionally.

During the spring of my senior year, I was busy interviewing for full-time positions after graduation. At one particular campus career fair, I came across the Z Insurance Corp. booth. As a business student, I had a keen interest in financial services. I believed and still believe that it is a noble profession, which helps to give hardworking people the power to be financially stable, save money for retirement, or put their children through college. Because of these interests, I was very curious to see what Z Corp. had to offer in the realm of financial services.

Looking back (with 20/20 hindsight), I believe that I was duped from the beginning. I'll tell you why in the following two actual scenarios.

Scenario One: "How I Learned to Lie to the Elderly"

My grandmother is one of the most caring and wonderful people I know. Recently, my grandfather passed away and left my grandmother with a considerable amount of money, and little financial experience to manage it. She guarded the money very carefully, since it was earned by her best friend and loving husband. Back to Z Corp.

The new "recruits" at Z Corp. have a two-week-long orientation before they can begin their work. During the first couple of days of this orientation, we watched films that illustrated how we would be helping senior citizens protect their life savings. These films had positive messages about America's senior citizens, including how to communicate with them in a respectful manner, cherish their money as if it was ours, and take each question they had with the utmost care. Although I was still a bit shocked by the fact that I was now an insurance salesperson, I was excited by the prospect of making a difference in the lives of America's senior citizens. I was picturing folks, similar to my grandmother, who would trust us to help them protect their life's hard-earned money.

These utopian ideals were soon transformed into harsh realities. Daily, I became increasingly aware of the games that this company was playing with us and the people that we were to "help." On one particular day, we were discussing how we were going to "entice" our customers on the phones so that they would listen to our message about long-term care insurance. Again, we didn't know that we were going to be involved in "cold calling," which was yet another surprise to us. During this meeting, we were given our "communication," which was to be followed very closely, not deviating from any of the scripts. While I was reading over the "communication," something struck me as peculiar. The following is a rough sample of our "communication":

Z Corp. Rep: "Hello, my name is Lea Stern from Z Corp. I am a financial adviser. I am calling in regard to literature that you received in the mail from us. Do you recall receiving this information?" (Usually the response was "No, I don't remember seeing anything from Z Corp.")

Z Corp. Rep: (*chuckling*) "Oh, I am sure you may not have. We all receive so much in the mail these days that you may have thrown it away or may have not read it yet."

After I read this script, I asked the sales manager whether or not these folks actually received something from Z Corp. regarding long-term care insurance. What he said in response to my question still rings clear in my head. So clear, in fact, that I am going to quote it: "These folks are old and confused. Most likely they received something in the mail about 'financial planning.' We are banking on the fact that they will not remember or realize who it was from and will take our word that it was from us."

"Old and confused" is how the sales manager described my loving grandmother. Because of the values that I grew up with and still hold, I could not imagine taking advantage of hardworking seniors in such a twisted, immoral way. With this one statement, I decided that I did not respect my manager or Z Corp. My attitude changed immediately. I knew from that moment that I would find it very hard to work for Z Corp. and almost impossible to work for that manager.

Scenario Two: "Reading the Fine Print"

I have been blessed with a wonderful family who surrounded me with caring people who would never try to take advantage of me. Maybe I am trusting and a bit naive, but I'm not stupid! With the experience I described previously at Z Corp., I learned that this trust could be a double-edged sword. I lived 21 years not realizing how twisted company policies and practices could be; it took only one week at Z Corp. for me to wake up to "corporate realities"—at least in an insurance-sales setting.

At the career fair at the University of New England, I had a wonderful conversation with a sales manager at Z Corp. We discussed the virtues of being a financial adviser, such as recommending appropriate mutual funds based on financial needs, careful investments, and the merits of having Series 6 and 7 licenses. I enjoyed the fact that Z Corp. seemed to be a company that helped folks invest in diversified ways. Never once were insurance sales, cold calling, or no pay for four months mentioned; not during the first, second, or final interview. Only when I signed on and was in training did I find out the truth about this shifty company.

During each of the lunches on that first week of our orientation, the "recruits" discussed what we called the "footnote." We used this term because we felt there was always another footnote regarding pay, customer contact, or office supplies. I felt as if I were employed at a different company, with a completely different position than the one for which I originally interviewed. Some of this may have been my fault. For example, I never asked what the values of this company were or what its mission was. However, important points such

as job function and company mission, as well as reimbursement, should be communicated truthfully. I felt as if the people at Z Corp. did not communicate effectively with us at all. A communication channel was not established between the managers and me at Z Corp. Without proper communication, I was taken advantage of and didn't feel comfortable being in the follower role. I didn't know what the company stood for, and most importantly I didn't know what I stood for!

Questions

1. What are your general reactions to the two scenarios?
2. Would you react similarly or differently than the writer? Explain.
3. Do you believe the writer is naive and that these scenarios represent the "real world" from which she has been sheltered? Or, do you think this company is a single "rotten apple" among the more honest companies in this industry and the writer should react as she did? Explain.
4. Are there any illegal or unethical tactics that the company sales manager/rep is using? Explain.

Real-Time Ethical Dilemma

Whose Values? Whose Decision?

Jim Howard is a sales manager at a software company that produces a search interface for databases with indexed information. The company is an established vendor and has a good reputation in the market for its high-quality products, fast and personal customer support, and strong loyalty to its customers. Part of the values statement of the company includes, "We will treat our customers with respect and dignity."

In his first year with the company, Jim noticed that the sales force was having difficulty acquiring new customers and retaining existing ones. The problem was complex: a shrinking market with continuously increasing buying power, increasing competition, and the emergence of free alternatives from the Internet. These problems started to significantly affect the company's revenue. The company's reaction was to drastically decrease the cost of its products, bundle databases into packages, and start to alter product introductions by including several value-added services that were new to the market.

Jim's boss suggested that Jim take over the responsibility for the yearly renewals of customer subscriptions from the company's secretary, which previously had been regarded as an easy clerical procedure. When he started to check the old accounts and follow up with renewals, he faced a problem that he thought would never have occurred: unfair treatment of old customers in comparison to new customers in terms of the product pricing. Existing customers were offered renewal at triple the price of the same package offered to new customers.

When he asked his boss whether he should inform the old customers that the price had changed and whether the old customers could now benefit from the lowered price, the answer was, "Why don't we try to get this price? If the customer refuses to pay it, then we'll negotiate." An additional difficulty was that, in the last few months, information had been disseminated to all customers that made the company's new pricing strategy visible to customers. Jim shared the fact with his boss that this information was already available to customers and pointed out the contradiction. His boss remained insistent, to the point of shouting, that Jim follow his previous instructions with the sales force.

Jim felt he was betraying the company, the customer, his sales force, and his own professional values. He didn't want to lose his job, and he didn't want to lose any more customer accounts.

Questions

1. If you were Jim, what would you do in this situation?
2. What are the issues here? For whom?
3. Who stands to be hurt the most from following the advice of Jim's boss?

4. What would a values-based stakeholder management approach suggest that you do, if you were Jim? Lay out an action plan and be ready to role-play your suggested approach.
5. Compare your answer to question 1 to your approach in question 4. Any differences? If so, could you still follow what you said in question 4?

Cases

Case 17

Kaiser Permanente: A Crisis of Communication, Values, and Systems Failure

In 2009, the customers of Kaiser Permanente (KP), a California-based health care organization that runs both managed-care hospitals and a medical plan (HMO), rated the company highest in the J.D. Power and Associates National Health Insurance Plan Study (SM) in four regions: California, Colorado, Northwest and Virginia–Maryland. In all four regions, the company ranked 40–50 points higher than the average score, measuring coverage, benefits, choice of provider, and administrative efficiency.

One factor, not directly included in the survey but cited as value added to the company, was the company's easy-to-use web interface that allowed users to schedule appointments, check and update medical histories, view and pay invoices, fill prescriptions, and otherwise access hospital and insurance records from home. The goal of information technology (IT) at KP was to connect all members of the network–patients, physicians, specialists, hospital and plan administrators, and other medical staff–while, at the same time, maintaining a customer-oriented focus. The customer satisfaction associated with the Web interface, called "myHealthManager," was extremely hard-won, however. In fact, KP's IT-related track record was erratic, at best. The company's IT goal and its inability to attain it would become part of an inconvenient company crisis.

A Company Crisis

> Dear Colleague,
> Three weeks ago, George Halvorson, our CEO, wrote to tell us that Health Plan and Hospitals are facing significant financial challenges. What Mr. Halvorson did not mention was the magnitude of the financial losses we could see: our internal projections show that we could lose as much as $7 billion dollars in total over the next two fiscal years. Losses of even a fraction of that total will be a threatening blow to our organization and what we stand for, and will significantly compromise our ability to care for our members.
> –Excerpt from an e-mail from Justen Deal, project supervisor at KP, sent on November 3, 2006.

On Monday, November 6, 2006, approximately 50,000 employees at KP discovered an e-mail from Justen Deal, a project supervisor working in the company's project education and training department. The e-mail was passionate but researched, thoughtful and committed to the company's core mission. The e-mail stated that KP's new electronic medical records (EMR) system, HealthConnect, was a failure; that it was unable to scale up to an organization the size of KP, that it was going to cost the company billions of dollars and might even jeopardize patient information and erode customer loyalty and trust.

The e-mail accused several top company executives, including Chief Information Officer (CIO) J. Clifford Dodd and CEO George Halvorson, of having a personal interest in HealthConnect's developing company, Epic Systems, as the vendor of choice and accused them of circumventing normal vendor procedures to ensure the selection of their product despite an internal engineering analysis that questioned the system's acceptability and scalability to a health care organization of its size and complexity. Justen Deal later stated that Halvorson was the main supporter of the Epic Systems choice and was canceling other internal CIS (Computer Information Systems) efforts at the time research into vendor possibilities was just beginning.

Despite the IT department's frantic attempt to remove the e-mail from the system over the weekend (the employee had sent the message late in the day on the prior Friday), the e-mail remained in inboxes throughout the company. To make matters even worse, those employees who received the e-mail on Monday morning almost immediately forwarded it to their coworkers, who then forwarded it to their coworkers. The number of people who had read the e-mail quickly grew from the original 50,000 to all 180,000 employees at KP (both those at the hospitals and those at the health plan). The e-mail was also leaked externally, setting off a stream of negative publicity and media attention. CEO Halvorson sent a company-wide e-mail on the same day dismissing the author's claims, but the damage had already been done.

The organization felt the effects of the e-mail almost immediately. Justen Deal, the author of the e-mail, was placed on paid administrative leave, his computers were seized, and the company initiated an investigation to determine if his e-mail violated company policy and could provide the basis for termination of employment. Deal would ultimately be fired, though the company would cite reasons other than his e-mail. On the Tuesday following the e-mail's dissemination, the company's quarterly report was published. J. Clifford Dodd resigned as CIO and was replaced by an interim CIO, Bruce Turkstra, who was the vice president and program director for KP HealthConnect at the time. In attempts to manage damage control, several staff members gave interviews attesting to the system's reliability. KP also paid Google to place an ad for the company at the top of any search conducted for Justen Deal's name. *Computerworld* magazine published a 722-page report on the weaknesses of the system, and a California health care watchdog group began to monitor the company.

The Whistle-Blower

Justen Deal was a 25-year-old project supervisor in the company's project education and training department. His department was involved in the testing of the new system and had access to reports related to HealthConnect and an understanding of its functionality. According to one report, the $1.5 million cost was noticed as incongruous almost immediately. He believed that the project had stalled as a result of its lack of scalability to an organization of KP's size and that the project had been chosen not because of its potential value to the organization, but because of management preference.

The e-mail itself was the result of many months of research. Prior to penning and distributing it, Deal spent several months trying to bring HealthConnect's possible fallacies to the attention of internal management. While he admitted that Epic was a good vendor with a great product, Deal did not see the vendor as a good fit to the organization. Furthermore, the system was suffering from regular outages due to data load. Deal informed an internal investigator of his concerns, but his concerns were dismissed. He then sent a letter to the company's chief compliance officer and all board members detailing his concerns and received a response that an investigation had been conducted and no indication of dishonest executive conduct or issues with project scalability had been found.

Deal had a history of activism. As a teenager, he testified in front of West Virginia's legislature in favor of gay rights. He studied journalism in college, but did not complete his degree. After leaving school, he worked for the West Virginia Symphony, a gay-rights group in West Virginia, a travel agency in Ottawa, and then KP.

Kaiser Permanente: A Brief Overview

KP is a nonprofit healthcare network based in Oakland, California. The organization consists of three functional units: Kaiser Foundation Hospitals, Permanente Medical Groups, and the Kaiser Foundation Health Plan, but considers itself to be a single organization. This view is supported by management. KP is run by CEO George Halvorson and a board of directors. Each hospital in the network is run by a managing physician or executive director.

KP is a managed-care organization (MCO), which means that members pay a fixed membership rate and then receive the right to services at any of KP's hospitals and clinics. "The essential difference between MCOs and more traditional types of medical care is connected with the distribution of financial risk among the purchaser of the health plan, the provider of the care and the insurer." The health plan primarily serves that membership, which numbers approximately 8.3 million.

The organization's mission statement is as follows: "At Kaiser Permanente, our mission is to provide affordable, high-quality health care services and improve the total health of our members we serve." KP is considered the largest MCO in the United States, serving Northern and Southern California, Colorado, Georgia, Hawaii, Ohio, and the Mid-Atlantic and Northwest regions. It also has a subsidiary company, KP International, formed to provide managed-care consulting services to companies and governments overseas, focusing on Asia, Australia, United Kingdom, and Eastern Europe.

KP's vision statement expresses the following values: operating as a team, valuing the contributions of its employees, exhibiting compassion and investment in the health and well-being of the membership, supplying superior health care value, partnering medicine and business, remaining first choice for a career in health care, fostering innovation, providing leadership to healthcare community and supporting the external community.

One challenge of the organization is balancing exceptional medical care with cost management. As a membership-based organization, it does not receive extra cash flow from specific medical procedures.

KP HealthConnect

The new HealthConnect system was, at the time, also in the testing and early rollout phase in a small number of hospitals in the Kaiser network. As of 2006, KP had not yet broadened its IT project scope to include a Web interface for its customers and was more concerned with internal data management. HealthConnect was designed as an internal tool to provide an information backbone for its 12,000 physicians, 30 medical centers, and 431 medical offices. The purpose of the network was to provide a centralized data management system to handle all medical records in the hospitals and through the plan (which directly served KP patients) electronically. This would reduce paper, data redundancy, and potential for errors and mistakes. It also would enable all physicians and other medical personnel to access patient data regardless of location, time of day, or urgency of need. The system was intended to centralize data from all locations to provide a common system for employee decision making throughout the network.

At the time, several other data management systems were already in place at KP. One such system was the Medical Automated Records System (MARS) used in KP-Ohio. This was a knowledge management tool that integrated "client/server technology, relational databases, intranet and extranet capabilities." MARS could be seen as a smaller-scale version of the HealthConnect system. It used a variety of interfaces and technologies to connect all Kaiser medical staff within the state with the information pathways and data centers necessary to provide quality care, while doing so in a cost-effective manner. It also provided care parameters to give users support to medically assist patients in ways that were proven, successful, and cost-effective. Its design enabled for extensive report-generating capabilities, which positioned the system to accommodate the requirements of the Health Insurance Portability and Accountability Act.

In 2006, MARS had received some acclaim as being strategically beneficial and innovative in the health care field, including recognition in a paper presented at the 35th Annual Hawaii International Conference in System Sciences by Nilmini Wickramasinghe from the James J. Nance College of Business Administration at Cleveland State University. At the time that HealthConnect was implemented, however, all work on this and other homegrown systems in conjunction with IBM had been discontinued.

The Health Insurance Portability and Accountability Act of 1996

One of the primary motivating factors for health care-oriented data management in recent history is the aforementioned Health Insurance Portability and Accountability Act (HIPAA) of 1996. This act provides a standard by which electronic medical data is handled, stored, and transferred. It affects which members in an organization are able to access, read, disseminate, and otherwise use the data. It also confers specific rights on health care consumers: the right to access to one's own records; the right to disclosure about an organization's privacy practices; transparency in regards to who has accessed one's records; and a limited right to privacy and a procedure for filing a complaint. HIPAA contains provisions regarding proper transmission and storage of health-related records and guidelines for

training those who handle this information on a regular basis or have access to storage locations. Health care providers and health plans that transmit information electronically are both considered covered entities under this Act. When it was implemented in 1996, HIPAA set a series of staggered deadlines for various levels of compliance. The final compliance deadline was April 21, 2005.

Medical information is only protected under HIPAA if it is connected to identifying information. That is, a doctor discussing a patient's condition in a general way is not covered, but if this information is in any way connected to identifying information (name, address, social security number), then it is covered under HIPAA. HIPAA's jurisdiction extends only to companies based in or conducting operations in the United States. Should information be sent to a business entity outside of the United States, HIPAA is not enforceable.

In February 2009, the Health Information and Technology for Economic and Clinical Health (HITECH) Act was signed into law. This is a provision of the American Recovery and Reinvestment Act of 2009 and provides federal stimulus money to advance the design and development of a national health care infrastructure. It builds upon HIPAA to outline much stiffer penalties for noncompliance with HIPAA and lays out much more extensive requirements and enforcements related to enforcement of patient privacy.

Other Data Management Issues at KP

HealthConnect was ultimately implemented on an organization-wide basis and is successfully used to the present time (with limited connectivity to the myHealthManager customer database). The fiasco detailed above was only one event along a continuum of negative public relations related to KP's IT initiatives, however. One of the most pressing concerns related to these initiatives is that of the privacy of its patient-members.

A major data privacy concern has existed for some time with regard to KP's outsourcing initiatives. In 2003, it was disclosed that the organization was quietly outsourcing computer operations to India to reduce overhead costs. The computer operations included data storage, transcription and retrieval regarding patient medical data, personal member information, and payroll information of KP employees and member physicians. The outsourcing plan called for remote access to KP's systems by at least six Indian firms. Although outsourcing of computer operations was an increasingly common trend for the health care industry, this news caused a furor in the media because some of the data transferred was sensitive patient data, and once the records went overseas they were no longer covered by HIPAA. Outsourcing firms do not qualify as third parties under HIPAA, and there have been many stories of employees of outsourcing firms who violated privacy guidelines through either negligence or intent–for example, in 2003 a medical transcriber in Pakistan threatened to post online patient records if the University of California San Francisco did not pay her back wages. In April 2009, KP announced that it had struck a deal with IBM to outsource the management and storage of most of its data to IBM, eliminating approximately 700–860 jobs and transferring its IT and data management out-of-house.

One of the most significant negative public relations events in recent history occurred when KP employees violated patient privacy laws by accessing the medical records of various celebrity patients without permission or reason. In March 2009, KP disclosed that 15 of its employees had illegally accessed the medical records of Nadya Suleman, the woman who gave birth to octuplets in their hospital in Bellflower, California, on January 26, 2009; these employees were subsequently fired. Two months later, the state reprimanded KP and fined the organization $250,000 for breach of privacy under the new HITECH law. "According to a report by California's Department of Public Health, the hospital did not do enough to prevent the violations." This fine followed a $200,000 fine in 2005 from the California Department of Managed Health for violation of both the Notification of Risk to Personal Data Act and HIPAA after a software test of an initial version of myHealthManager accidentally made confidential patient information accessible on a public web site.

The IT/data management issues presented in this case are part of a continuum of ongoing threats and challenges to the integrity of the IT/data management systems and policies in place. Due to the interconnection of data management practices and policies with patient care practices and policies, challenges to the integrity of the data management system affect and reflect directly on the rights, lives, and humanity of those served: patients and employees, executive decision makers, subsidiaries and business partners, and the communities in which the organization functions.

Conclusion

KP's data management-related crisis cycle highlights the inherent dichotomy between its stated mission's focus on patients and the autonomously functioning business goals that appear to operate based on a mind-set that is both pragmatic and individualistic. The dysfunction between the two sets of values appears to create an ethical vacuum within the organization, in which decisions are not made based on a core set of values or principles. Due to the lack of shared purpose and a code of ethics, the company appears to be unable to break out of the continual cycle of crisis and clean-up involved in the disclosure of misbehavior or even illegality within the health care network and is unable to achieve a level of organizational self-awareness that would allow it to adopt a proactive ethical stance against internal wrongdoing and effectively conclude their crisis management cycle.

Questions for Discussion

1. Do you think a company-wide e-mail was the best way for Justen Deal to express his concerns about the HealthConnect system? Why or why not? If not, how should he have handled the situation?
2. Are there any concerns about top company executives personally investing in company vendors? Explain. Imagine that you were the director of IT at Kaiser Permanente. What would you have done about the e-mail sent to employees? Do you think it was right for IT to remove the e-mail from the system? Why or why not?

3. What responsibility, if any, should Kaiser Permanente have taken over the actions of its third-party outsourcers with regard to the protection of private patient data? Explain your answer.
4. In your opinion, how well did Kaiser Permanente manage the crisis of Justen Deal's HealthConnect e-mail? Using a crisis management framework from Chapter 3, evaluate the crisis in this case and offer suggestions for what should have happened and why.

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Case 18

Social Networking and Social Responsibility

The Beginnings of Social Networking

Early social-networking web sites started in the form of generalized online communities such as The WELL (1985), Theglobe.com (1994), Geocities (1994) and Tripod.com (1995). The goal of these online communities was bringing people together to interact in virtual "chat rooms" to share personal information and ideas, which served as the start of the "blogging" phenomenon. These sites included Classmates.com (1995), focusing on ties with former peers, and SixDegrees.com (1997), which focused on indirect ties. The sites had the capabilities of creating user profiles; sending messages to users stored on a "friends list"; and searching for other members with similar interests in their profiles. Although some of these features predated these web sites, this was the first time such functions were available in one package.

Between 2002 and 2004, four social networking sites (SNSs) emerged as the most popular form of these sites in the world: Friendster in 2002 (which Google tried to acquire in 2003), MySpace and LinkedIn a year later, and finally, Bebo. By 2005, MySpace had emerged as the largest such site and was reportedly getting more page views than Google. Facebook emerged in 2004 and grew exponentially. In 2005, Facebook opened to the non-U.S. college community and created externally developed applications that enabled graphing of a user's own social network and the capability of linking social networks and networking.

A Growing Global Trend

Social networking continues to be one of the fastest-growing global trends. According to Pew Research Center's Internet and American Life Project, "the number of those using social networking sites has nearly doubled since 2008 and the population of SNS users has gotten older." Fifty-nine percent of Internet users claim to use at least one SNS—92% of SNS users use Facebook, 29% use MySpace, 18% use LinkedIn, and 13% use Twitter. Most people in the world today have either heard of or actively use Facebook, Twitter, MySpace, LinkedIn, or one of the many other SNSs available to the public. Common uses for social networking include: staying connected with fellow users, following world news and gossip, and sharing opinions and life experiences. SNSs, however, are being used for commercial purposes often unknown to the user.

Social Networking in the Corporate World

Businesses gravitated toward social networking as an innovative marketing strategy around March 2005 when Yahoo launched Yahoo! 360°. Various SNSs have since sprung up catering to different languages and countries. It is estimated that there are now over 200 SNSs using these existing and emerging social-networking technologies. This number does not include the niche social networks made possible by services such as Ning. Twitter, launched in 2006, has eclipsed

many other social network services, even though it lacks some features that were considered essential aspects of a SNS.

Social networking allows businesses to place their company information within an online network to build contacts and relationships with individuals that share the same interests and insights. It creates an outlet for interactive communication using online communities. The tools available also allow businesses to reach millions of people in a short amount of time, usually with no cost attached.

Companies have found that SNSs such as Facebook and Twitter are great ways to build their brand image. According to Jody Nimetz, author of *Marketing Jive,* there are five major uses for businesses and social media: 1) to create brand awareness; 2) as an online reputation management tool; 3) for recruiting; 4) to learn about new technologies and competitors; and 5) as a lead-generation tool to intercept potential prospects. These companies are able to drive traffic to their own online sites, while encouraging their consumers and clients to have discussions on how to improve or change products or services.

Companies and advertising firms use the sites to analyze consumer trends, opinions, and influence consumers to view their products favorably. Is this practice of tracking user information without their knowledge ethical? Some companies might state that they are simply trying to leverage social networking to create a creative work environment for their employees and offer a better product to consumers. IBM is a company that uses social networking in both ways. The ethical implications of social networking and consumers as influencers are much clearer when we take a closer look at how a company like IBM uses social networking in its daily operations.

Social Networking at IBM

International Business Machines, or IBM, is one of the most notable companies operating in the world today. According to their company profile, IBM was founded in 1910 and currently employs over 440,885 full-time employees in 200 countries tasked with manufacturing and selling computer hardware and software, as well as infrastructure, hosting, and consulting services in areas ranging from mainframe computers to nanotechnology. The company's five segments of operations include: Global Technology Services, Global Business Services, Software, Systems and Technology, and Global Financing. IBM, as a world leader in computers and computer software, has a unique method for understanding and applying new technologies for solving technical business problems and leveraging new technologies in the technology sector. The use of social media and social networking is no different. Companies continue to find ways to use social media sites like Facebook and Twitter to increase their bottom line. At IBM, social networking has already been implemented to generate new ideas, increase employee morale, monitor consumer trends, and increase visibility and sales for the company.

Social networking at IBM is publicly advertised as a creative and innovative way to keep employees connected and keep the company in tune with consumer demands. The framework for internal social networking among IBM employees

is an employee-edited directory known as "Blue Pages." This directory is used over 6 million times a day by 400,000 IBM employees to access information on other employees and send them instant messages. Employees at IBM have control over their profiles and can add photos, resumes, or other personal information to foster a sense of community with other IBM employees. The company points to the sharing of ideas or opinions on new technologies and developments as one of the main advantages of such a site.

IBM also offers an internal network space where employees can post blogs for other employees to read. Blog topics range from personal opinions on various technologies to updates on work that is being done by different groups within the company. The blogs offer a unique way for employees to communicate with each other and keep current on company events.

Wikis

Another element of social networking within IBM is information-storing web sites called wikis. The leaders of the various software production teams at IBM manage these wikis and allow team members to share memos and other information for the entire team to view. Each team member can share his or her progress with the other team members through these wikis, allowing team leaders to monitor the entire project without having to contact each team member directly. The major advantage of this outlet is that IBM employees may work from home or other locations without having to travel to a single destination in order to complete a project. This is especially important for the 42% of IBM employees that regularly work from locations other than IBM facilities.

IBM has a policy in place that strictly forbids any employee from joining the company's social-networking platforms anonymously. This ensures that every comment or post made by an IBM employee is transparent to other employees in the company. The onus is on the employees to police themselves and forward any inappropriate comments or posts to upper management.

While these social-networking tools attempt to connect employees, IBM has also leveraged social media to stay connected with customers. IBM developed a social media monitoring software known as the SPSS Modeler, which the company uses to search for customer comments, sentiments, and opinions on various social-networking platforms like Twitter, Facebook, and online blogs. This tool can mine through large piles of data searching for specific text, industry terms, or developing technology that may be pertinent to IBM's customers. IBM uses this information to stay up-to-date with the latest trends and consumer behaviors. If consumers have positive or negative opinions about IBM products, the company can track the feedback and make changes accordingly.

IBM has also developed a software known as Cognos Consumer Insight, which can perform predictive analytics on the text and data that the SPSS Modeler can pull from Twitter, Facebook, etc. This technology takes the data collected by the SPSS Modeler from the SNSs, analyzes the consumer sentiment, and makes predictive analytical decisions based on the information it is viewing. In essence, the computer software is a form of artificial intelligence that performs

the job of marketing analysts. IBM uses this software internally, but also sells it to other large companies and retailers, along with the services necessary for these companies to learn how to analyze the data. Some companies already using this IBM technology are Rosetta Stone, Navy Federal Credit Union, and Money Mailer.

The ingenuity and resourcefulness displayed by IBM leveraging social media tools to enhance their business is a reminder that thinking creatively can benefit even the largest companies. The use of social networking within the company helps to generate new ideas and develop a sense of camaraderie among the employees at minimal cost to IBM. Employees are allowed to develop a personal identity and share their stories and experiences through blogs and personal profiles. For a company that thrives on creativity and new technology, social networking is the perfect way to share ideas and opinions without the limitations that come from simple e-mail correspondence.

Using Social Media for Consumer Data Collection

The ethical implications of using social networking to monitor consumer demands are far more complex. Unlike using social networking internally to generate discussion among employees bounded by rules and policies, external uses of SNSs allow IBM to monitor what consumers are saying without consumers knowing that they are being monitored. Although this is not an illegal practice because the information is publically posted on social media platforms, the question must be asked, is it ethical? IBM is openly developing and selling their software to other companies so that they, too, can track consumer sentiment through social networking and make key business decisions based on information that consumers are sharing on the Internet. The term used by IBM's vice president for social business and collaboration solutions, Sandy Carter is "analytics." Carter prefers to focus on the positive results that social networking has within the company, but also admits that analytics has become a key component of "tracking sentiments, and finding out how the community is feeling about an issue." She goes on to say that IBM uses "deep analytic capability to find out what is being said. Then we look at affinities." IBM can track users tweeting about the company, users that are the most influential tweeters, and so on. Tracking these types of postings allows the company to make decisions based on consumer feedback without the consumers ever knowing that they influenced the decision. Carter does not condemn the company's decision to use social media to analyze consumer decisions, and justifies the practice by making the argument that whether or not your company participates in social media or monitors consumer sentiment, most brands are already openly discussed by consumers, so you might as well monitor what they are saying.

Legality of Social Networking

As social networking grows rapidly, the debate over legal implications of using various social-networking tools continues. IBM is using social networking to support internal innovation and form a closer bond among its various departments. At the same time, the company is attempting to deflect the focus from its other

uses of social networking that include developing and using software to track customer sentiments and influence consumer behaviors. From a legal standpoint, IBM is not violating any existing laws, but social networking is an area in which laws are constantly evolving. Most of the laws in existence today protect social-networking companies from lawsuits brought on because of information that users have posted on their pages. These types of lawsuits would be relevant to companies like Facebook and MySpace, where users share their opinions and ideas to a larger community. Although IBM encourages their employees to write blogs and share information on their personal profiles, any content that is displayed by employees must adhere to the IBM code of conduct.

The major hurdle for IBM regarding their external data analytics practice revolves around the privacy issues that SNSs now face on a regular basis. Sites such as Tagged and Facebook have come under legal scrutiny for using members' e-mail address books to solicit new members, or for broadcasting members' transactions with affiliated web sites on their Facebook pages. The lawsuits these SNSs faced were based on the premise that the consumer or user has certain rights to privacy that these companies violated. If companies like Facebook are coming under fire for breach of privacy, how does IBM get away with monitoring user information and using it to influence consumer decisions without their knowledge? Although no laws currently exist to prevent IBM from continuing this practice, changes are being made by the government and SNSs themselves to slowly limit intrusion into personal information. Companies that participate on SNSs have the same potential liabilities as any one of us has, including copyright infringement, trademark infringement, and defamation. Analyzing information that users openly disclose on their profile pages to influence business decisions is not considered illegal because it is the users' job to withhold any information that they do not want companies to see.

A person who has a Facebook page and openly shares opinions or personal information on that page is giving Facebook ownership of his/her photos and postings; and, accepts the fact that information is publically viewable. Monitoring practices have come under scrutiny by individual users and consumer rights groups, but few lawsuits have challenged this type of data collection. Any lawsuits that have challenged it are usually directed at the SNSs themselves for failing to maintain certain levels of user privacy. Because social networking is a relatively new trend whose potential is not fully understood, the legislation governing this type of technology is not yet up to pace with its rapid growth and expanding capabilities.

It is feasible that within the next 10 years, Sandy Carter and executives at other companies will not be able to rely on social media for consumer analytics. In 2010, the Federal Trade Commission (FTC) made it clear that federal regulation may be necessary to protect the private information of consumers if self-regulation fails. At the same time, the U.S. Judiciary Committee has passed the Personal Data Privacy and Security Act and the Data Breach Notification Act, which broaden consumer privacy rights regarding information collected and distributed by "commercial data brokers." These data brokers are the types of companies to which IBM sells its analytic software.

IBM uses social networking both internally and externally, and the ethical implications of those uses are significant. The company openly promotes its usage of internal file sharing and blogging, but all employee actions are guided by IBM's ethics codes and value statements. IBM's use of analytics to monitor consumers is technically legal, but ethically questionable.

Ethical Implications

IBM is one of many large firms that uses analytics in its day-to-day operations and continues to develop analytic software for other companies. The company also promotes the use of social-networking tools to share ideas and connect with different groups operating in the company. A question still remains about whether or not this and other practices are ethical.

Ethical implications may be considered from two angles: the internal and external organizational uses of social networking. A company's use of social networking to pass along ideas and share personal information internally may be ethical and morally acceptable if no harm is done to any user or the company. Employee stakeholders interested in developing new ideas and increasing wages and benefits may help the company with their contributions using social media. Customers and customer advocacy groups may also be interested in purchasing a product that lives up to its stated advertised online purpose and that functions at or above the promised level. Those government, political groups, and competitors that are interested in ensuring that organizations operate in fair and legal ways would be observant of the ways social media methods are used with external groups, including consumers. Stockholders, suppliers, vendors, and companies also have a stake, not only in maximizing their profits through using social media, but also in acting socially responsible toward each other to ensure business growth, while protecting consumers and the environment.

Using social networking to share ideas and information with other employees or departments internally also aligns with the responsibilities and moral obligations a company has to its various stakeholders. Sharing new thoughts and ideas with others through social-networking software can potentially increase opportunities for successful innovation and product development. Additionally, as employees connect with each other at human and communal levels, morale and motivation to act ethically increase.

Darker Sides of Social Networking

Using social networking to monitor consumers and analyze trends without their knowledge is a different matter, one that is ethically questionable. Legally, using data collected by consumers to analyze and influence certain business decisions is permitted, but the legislation protecting consumers is constantly changing and evolving with technology. As quickly as the legal system is working to catch up with technology, it could be a practice that is illegal in a matter of years.

Corporations have an ethical responsibility to inform consumers; not misrepresent or withhold information from consumers; not force or take undue advantage of consumers; and take "due care" to prevent any mishaps. Based on this framework,

companies like IBM are acting unethically by using social networking to perform customer analytics. First and foremost, the very nature of collecting data from Facebook and MySpace without letting the customer know that they are doing so breaks the first rule of informing the customer. If customers are aware that they are being monitored and permit companies to collect data from their accounts, then there may be no legal or ethical issues. An alleged argument about some data-collection methods used in analytics to collect unbiased information, is that this process can occur without consumers' awareness. Corporations also have a responsibility to not misrepresent or withhold information about a product or service that would hinder a consumer's free choice. By setting up corporate SNSs and then luring consumers to view the pages through daily deals, games, and prizes, the corporation would be withholding information from the consumer. A person without specific marketing knowledge might think that playing a game or leaving a comment on the Facebook page of a company is of little or no consequence. Meanwhile, the company is collecting and analyzing such activity while strategizing how to translate a product or brand into a consumer need and choice.

A major aim of ethical reasoning is to gain a clear focus on problems to facilitate acting in morally responsible ways. In this case, the company that is knowingly collecting information from consumers without their knowledge is morally responsible for the harmful effects of their actions when they knowingly and freely acted or caused the act to happen and knew that the act was morally wrong, or if they knowingly and freely failed to act or prevent a harmful act, and they knew it would be morally wrong for a person to do this. Companies like IBM that choose to monitor Facebook, Twitter, and MySpace for data may walk a thin line between providing consumers with desirable products and violating consumer rights. Government agencies such as the FTC work towards protecting consumers from certain acts by providing laws to promote consumer choice, and protecting consumer privacy. Specifically, the FTC has certain guidelines represented in the FTC Act that allows it to work towards preventing deceptive acts. In Section 5 of the act, the term "deceptive" is defined as a practice that is misleading to consumers, or one that affects consumers' behavior or decisions about the product or service.

Advancements in technology have certainly blurred the lines between what is right and wrong, ethical and unethical. A major issue with regard to the ethical implications surrounding the use of technology in the business world is that technology seems to advance much more quickly than related legislation.

Questions for Discussion

1. What are the benefits and risks associated with a company's use of social networking?
2. Are there any significant differences between a company's use of social networking technologies and an individual use?
3. As a social media user, are you concerned that your information is tracked for "advertising" purposes? Why or why not?

4. Compare IBM's private social network Blue Pages with a public social-networking site like Twitter or Facebook. Do you think user information is any safer on Blue Pages? Why or why not?
5. What responsibilities do companies have regarding private company social-networking sites?
6. Do you think it's right for companies to collect and analyze user data from social-networking sites in order to influence consumers? Why or why not?

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7

EMPLOYEE STAKEHOLDERS AND THE CORPORATION

7.1 Employee Stakeholders in the Changing Workforce

Ethical Insight 7.1

Point/CounterPoint

7.2 The Changing Social Contract between Corporations and Employees

7.3 Employee and Employer Rights and Responsibilities

Ethical Insight 7.2

7.4 Discrimination, Equal Employment Opportunity, and Affirmative Action

Ethical Insight 7.3

7.5 Sexual Harassment in the Workplace

7.6 Whistle-Blowing versus Organizational Loyalty

Chapter Summary

Questions

Exercises

Real-Time Ethical Dilemma

Cases

19. Preemployment Screening and Facebook: Ethical Considerations
20. Women on Wall Street: Fighting for Equality in a Male-Dominated Industry

Notes

OPENING CASE

Two Profiles

Profile of the New (Younger) Workforce

"Stand back all bosses! A new breed of American worker is about to attack everything you hold sacred: from giving orders, to your starched white shirt and tie. They are called, among other things, 'Millennials.' There are about 80 million of them, born between 1980 and 1995 [others say between 1982 and 2003], and they're rapidly taking over from the Baby Boomers who are now pushing 60."[1] "We are beginning to see increasingly younger people come in and ask long-term questions; five years down the road, where can I grow in this company? This was not necessarily the case with Gen X [people born between 1964 and 1981]. There is also a greater emphasis on bonding within an institution. Some companies are actually having camps and retreats where

they immerse people into living with one another 24/7 (like Accenture), learning the lore of the company. This would not have gone well with Gen X. This would have caused a riot with the Boomers, and Gen X simply wouldn't have been interested. . . . Employers hate the parental presence, but it is now extending into the workforce. . . . Excessive parental involvement was originally the single biggest complaint among teachers several years ago, then it predictably moved into colleges, and now it is becoming a pervasive issue in HR [human resource] departments with parents doing everything from helping fill out applications to actually coming to their children's interviews. . . . Many employers are working with this trend . . . employers are now working on co-marketing to parents."[2]

Second Profile of the New (Older) Workforce

"Shirley Serey is the community college student of the future: 59 years old, MBA, corporate manager, breast cancer survivor—and new teacher of special education, helping fourth and fifth graders with disabilities learn to read. . . . Serey is at the leading edge of tens of millions of Baby Boomers who are beginning to shift into a new phase of life and work. As many as four out of five people in their 50s and 60s say they expect to continue to work, some because they have to for financial reasons, but many more because they want to, for the social connections, intellectual engagement, and fulfillment of making a difference. Neither old nor young, many are seeking 'encore careers' that combine a renewed commitment with continued income and increased flexibility. . . . Shirley Serey is typical of the target market for such encore colleges. Her story weaves several themes common to boomers managing transitions to this new stage of life—the need for flexibility, the unexpected obstacles in the search for meaning, an impulse to give something back, to help other people, and to make a direct and noticeable impact."[3]

Employers and employees are experiencing a different mix of values, styles, and dilemmas in the changing workplace, as the above scenarios indicate. A review of workforce trends also indicates significant changes at the societal level, for example, "the Department of Labor must work with a wide spectrum of job seekers, including those with special needs such as the disadvantaged, people with disabilities, veterans, disadvantaged youth, and those who have lost their jobs due to foreign competition. Addressing the job seekers' needs is further complicated by the dynamics of the changing workplace. New technologies, increased competition, and changing labor markets have prompted employers to downsize, change employment patterns, and seek alternative labor sources such as qualified foreign workers."[4] A 2011 policy summit on America's "workforce mosaic" revealed that "America's workforce is currently being shaped by three converging trends: rapid growth in the non-white population, baby boomers who are staying in the workforce

longer, and veterans returning from the ongoing wars in Iraq and Afghanistan." UNC research shows that "79 million baby boomers will exit the U.S. workforce over the next 20 years." This graying workforce will result in some significant losses of experienced and top-level employees of large companies and a potential shortage of American workers.[5]

This chapter addresses the following questions: What is different about today's workforce, and how does this affect the corporation's ethical responsibilities? What, if anything, binds employees to their companies these days? What is the changing nature of the employer–employee social and psychological contract? How has this contract changed historically? What are the boundaries of employee loyalty? When do employees have the right or obligation to "blow the whistle" on a company?

A number of issues that employees and employers face are also presented, such as dating in the workplace, same-sex marriage rights, types of discrimination, drug testing, Internet use, privacy, and sexual harassment. The rights and responsibilities of both employers and employees are discussed with the aim of offering perspectives on what stakeholders can expect and how ethical dilemmas can be prevented and solved, beginning with an awareness of these issues. Creating a legal and ethical working environment where mutual respect and concern create conditions for productivity and human development is a worthy goal.

7.1 Employee Stakeholders in the Changing Workforce

The forces of globalization, deregulation, shareholder activism, and information technology continue to influence business practices and processes, as discussed in the previous chapters. Industries and companies are downsizing, restructuring, merging, and reinventing their businesses. Mid-level management layers are being pressured, many diminishing. Functions are being outsourced, offshored, eliminated, and replaced by online automation, cheaper international labor, and networked infrastructures. Knowledge workers with technological and people skills must manage processes and themselves in cyberspace with speed, efficiency, and accuracy.

Within the context of the "digital economy," the following changes with employees and professional stakeholders continue to occur:[6]

- An increasing shift to knowledge work, which increases the potential for satisfying work but heightens stress.
- The concept of "a job and career for life" is dead or dying. An employee holds nine jobs by the age of 30. Professionals are changing careers five to eight times on average during their working lives. Compensation, income, and the social distribution of benefits, including health care, are pressured by changing national and global economic conditions. Decreases

workplace policies. This information, although subjective, is used to develop workplace strategies and to evaluate ethical principles and beliefs of different groups in the workforce.[12] The following brief summary of five generations' dominant value orientations highlights some of these differences. As you read the descriptions of generational profiles, turn again to this chapter's Real-Time Dilemma to help explain possible sources of the conflict and potential organizational issues and dilemmas that are about to erupt.

- *GI Generation (born 1901–1925).* This generation survived the Great Depression and served in World War II. Members of this generation are churchgoers and belong to clubs and professional organizations. They express rugged individualism but are members of many groups. They tend to believe in upward mobility, civic virtue, and the American Dream.
- *Silent Generation (born 1926–1945).* This generation was too young to fight in World War II. They were influenced by the patriotism and self-sacrifice of the GI generation, from whom they did not wish to differentiate themselves. Their dominant principles are allegiance to law and order, patriotism, and faith. The Silent Generation likes memorabilia such as plaques, trophies, and pictures of themselves with important people. Most members are already in some form of retirement (i.e., fully retired or working part time, occasionally or seasonally to bring in some additional income).[13] If nothing else, the title promised a look at an era long gone: the 1950s; that is, the object of knowing derision today buried in clichés about a time when America was the land of happy automatons—a people unthinking, accepting, and repressed. The 1950s were characterized by serious, non-revolutionaries, and jobs- and marriage-focused young, in stark contrast to the more colorful decades to come—years of riots, bomb-throwing, seizure of the universities and the reign of the Weathermen.[14] This generation is characterized by "giving back and contributing to the collective good."[15]
- *Baby Boomers (born 1945–1964).* This is currently the most powerful demographic generation, with approximately 77 million members. They have led and set trends in society. They distinguish themselves from the former generations by assuming debt. Their "buy now, pay later" belief characterizes their instant gratification practices. They can be moralistic, but they question authority and the moral and ethical principles of institutions. They do not "join" or sacrifice personal pleasure for the good of the group or collective. They mix and match religious traditions and avoid the dogma and teachings of single religions. Baby boomers value health and wellness, personal growth, involvement, public recognition, status symbols, first-class travel upgrades, visible roles such as speaking at an industry trade show, and any type of resort or retreat. As employees, they are "process-oriented and relationship-focused."[16] Baby Boomers (who represented 44% of the working population in 2012) have the lowest level of engagement, and they have the highest level of active disengagement—nearly one in four are actively disengaged. Because this generation makes up such a large part of the working population, and many may be in the workforce long past

the traditional retirement age, a targeted effort to raise these workers' engagement levels could have important ramifications for companies and the overall U.S. economy.[17] More so than other generations, Baby Boomers respond to managers who make an extra effort to show that they care. Managers should keep this in mind during day-to-day interactions and find ways to communicate interest in these employees by inquiring about their work and other important aspects of their lives.[18]

- *Generation X (born 1965–1981).* Known as the "Baby Busters," this generation has 41 million members. Sandwiched between the two larger generations, they feel demographically overlooked. They came from a time of high national debt and bleak job markets, and were labeled as the "McJob" generation—a phrase referring to holders of low- and entry-level jobs. This generation generally believes that they will get less materially than the boomers. Insecurity is a dominant theme for X-ers, who value close friends and virtual families more than material success. They, like the boomers, are also suspicious of institutions. They experience their journey through life as one that changes rapidly and continuously.

- *Generation Y (born 1982–2003).* The millennial generation (or "Echo Boomers") numbers about 80 million. They spend $170 billion a year of their parents' and their own money and comprise one-third of the U.S. population. They have grown up with television, computers, instant messaging, and new technologies, just as the Boomers grew up with the telephone. Y-ers don't want to be associated with X-ers, whom they believe are selfish and complaining and the least heroic generation—a bunch of "slackers." Y-ers started growing up with a strong job market. They are ambitious, motivated, extremely impatient and demanding, and have a sense of entitlement.

  This group is also extremely practical. They welcome clear rules and guidelines, and display high levels of trust and optimism. They are keenly aware of current events and are sensitive to their surroundings. They define success in terms of team rather than individual achievement.[19] Millennials place a high priority on workplace culture and desire a work environment that emphasizes teamwork and a sense of community. They also value transparency (especially as it relates to decisions about their careers, compensation and rewards). They want to provide input on their work assignments and want and need the support of their supervisors. Millennials also are particularly attuned to the world around them, and many want the chance to explore overseas positions. All of the above statements also are true of non-Millennials, yet not to the same degree as the Millennial generation. With regard to ethics, members of this generation observe fewer boundaries than previous generations; are more flexible about when and where to apply boundaries; are more open, transparent, flexible; are more likely to discuss work activity with private and public people; are more likely to engage in and tolerate behavior that is unacceptable; are a more at-risk generation than the others, and, therefore, are more likely to observe misconduct and experience retaliation after reporting it; are more likely than older

generations to use ethics and compliance officers; and are more likely to respond to ethics and compliance programs that include social interaction and support (training, advice, helplines).[20]

Generation Y is more positive than other employee groups and is more likely to agree that "senior management communicates a clear vision of the future direction of my organization." They:

- have more favorable views on workplace issues, from work–life balance to performance reviews, to having access to their immediate supervisor.
- value teamwork and fairness and are more critical than other age groups on issues of fairness and cooperation.
- want to be challenged at work.
- are motivated less by money and more by opportunities to advance and have a life outside of the office.
- are concerned about tuition reimbursement and flexible spending accounts for dependent care.

Over half of Generation Y-ers would leave their organization to work for an organization that offered better benefits.[21] At this point in their careers, Millennials are generally more upbeat about all aspects of engagement than are Baby Boomers or Generation X members, but Millennials are particularly more positive about growth and development opportunities. Despite their higher engagement levels, Millennials are the most likely of all generations to say they will leave their company in the next 12 months if the job market improves. More than one in four of these young workers strongly agreed with this statement when asked in 2012.[22]

From a manager's perspective, Generation Y employees require "super-high maintenance," since they are "on fast-forward with self-esteem." They often expect office cultures to adapt to them. With these attitudes, they generally require coaching, rigorous feedback, and smaller and more realistic goal setting, with deadlines and increasing responsibility.

From the employer's perspective, integrating individual and group differences in the workforce requires, as mentioned earlier, leadership, planning, new policies, and training. In larger, more complex organizations, providing education and training to integrate the workforce is a necessity.[23] With which of these values do you identify? What other values that are not listed here motivate you? Underlying individual values combined with other background factors influence perceptions, beliefs, behaviors, and ethical decisions.

Steps for Integrating a Multigenerational Workforce

Generational differences may be only one among several issues that cause conflict and ethical dilemmas in the workplace. Using communication skills and emotional intelligence (managing self, others, and relationships with awareness and sensitivity) are important. Here are steps that employers can use to help diagnose, prevent, and resolve misunderstood generational differ-

ences. If you are not a boss, team leader, or supervisor, read these steps as if you were one. Taking this perspective can help you see the larger picture outside of a particular generational lens.[24]

Identify the Problem Areas

Where do I see the problems? Where do I expect to see the problems? Is there resentment about special treatment to senior or younger members in the workplace? Are the problems between individuals or groups from different generations? What are the sources of the problems: value differences, rewards, motivation, work methods, other?

Get To Know the Individuals Inside Their Roles and Positions

For Millennials and Gen X-ers, as well as members of other generations, it is important to arrange for conversations to discuss broader topics and subjects that are important to them. Do not wait for employees to come to you; it is important to plan, arrange, and invite individuals to conversations where needs and perceptions can be shared in nonthreatening ways. Being able to listen to the other's views, opinions, and perceived or experienced issues will help you understand the person and his or her issues. These are necessary first steps that lead to problem resolution.

Understand and Anticipate Expectations of Different Generations

"One size (of leadership or management) does not fit all." Although individuals must be recognized and treated as the unique individuals they are, it is also important for managers to seek balance between the employee and the company. Knowing generational members' expectations is important in negotiating this balance between responsibilities and obligations. "This can be achieved when a company (1) does not ask too much of its employees and (2) knows what it's willing to give employees *before* they've been given too much."[25]

Develop a Personal Growth and Development Plan for Each Employee

Millennials and Gen X-ers value and enjoy learning and benefit from their work when they are engaged. Assisting them to develop specific future goals and marketable skills is motivational and will focus their high work ethic and energy toward positive effort and outcomes.

Engage and Communicate

Younger entrants into the workforce are accustomed to being engaged, not mandated or reprimanded in an authoritarian way. Seek their input and advice. Conflicts between Gen X-ers and Millennials often occur when the former try to take charge over the latter. Neither likes to be told unilaterally what to do. If reprimands or criticisms are necessary, these can best be communicated one on one, as soon as a wrong action is done, and as objectively as possible. Reverse mentoring and mutual mentoring are two newer ways that Gen X-ers and previous generational types can learn from younger professionals. These more recent forms of mentoring can be effective ways of sharing and

learning different professional values and work ethics. Generation X, Millennials, and Baby Boomers are all most engaged when they have the opportunity to do what they do best every day. Engagement for Millennials, Generation X, and Baby Boomers is connected to having a strong sense of what their organization stands for. Find ways to help these employees verbalize and internalize what the company's mission and purpose means to them.[26]

Be a Leader, Not a Friend

Gen X-ers and Millennials are looking for role models in organizations, not buddies in a boss. Both generational members want to be led, since they generally have friends. This does not mean that they want to be led by authoritarian or unreasonable leaders. Character counts. Gen X-ers and Millennials move toward bosses who have strong character. They know when they see strong character. For effective managers, character means, "Do what you say and say what you do" in a reliable, trustworthy way and "Do the right thing"—although it may not always be comfortable.

Ethical Insight 7.1

Bridging Diversity Gaps in the Workplace

Do Companies Use Mentoring Programs and Why Are They Significant?

- 71% of Fortune 500 companies and 76% of Fortune's top 25 companies operate a mentoring program.
- *Promotion*: 75% of executives point to mentoring as playing a key role in their careers; and 44% of CEOs list mentoring programs as one of the three most effective strategies to enhance women's advancement into senior management.
- *Productivity*: Managerial productivity increased by 88% when mentoring was involved, versus only a 24% increase with training alone.
- *Development*: More than 60% of college and graduate students listed mentoring as a criterion for selecting an employer after graduation; 96% of executives say mentoring is an important development tool.
- *Retention*: 77% of companies report that mentoring programs were effective in increasing retention; 35% of employees who do not receive regular mentoring look for another job within 12 months."

New and Changing Types of Mentoring Programs

The old mentoring model assigned a younger professional to a more senior professional for an indefinite time. The following programs reflect new trends:

- *Short-term, goal-oriented mentoring:* Mentor/mentee are paired with specific goals that have time limits.
- *Peer-to-peer mentoring:* Young employees are paired together.
- *Speed mentoring:* Mentor/mentee are paired in restricted time-bound sessions for quick-hit information and networking, e.g., one hour.

- *E-mentoring:* E-mail is the medium between paired mentee and mentor.
- *Reverse mentoring:* Senior executives' mentees are paired with younger professional mentors to help senior executives catch up on new practices.
- *Job-fit-related mentoring:* Particular mentors and mentees are assigned to work on specific jobs.
- *Mutual learning, adaptation, and change:* Mentor and mentee are paired based on a learning partnership aimed at mutual growth and development.

Questions

1. Which of the above types of mentoring programs might help ease the potential ethical dilemmas in this chapter's Real-Time Dilemma?
2. Suggest how one or more of the mentoring programs here might be arranged by Ralph the CEO to help Bill and Lana's working relationship.

Sources: Katz, N. (February 2007). Enhancing effectiveness in mentoring. *Nation's Cities Weekly.* http://www.insala.com/Articles/leadership-coaching/mentoring-current-trends.asp, accessed April 22, 2014.

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Women in the Workforce

In 2011, women accounted for 47% of all employed persons 16 years of age and older.[27] In the same year, 58.1% of women were in the labor force, down 0.5% from 2010.[28] Overall, however, this percentage has increased from 43% four decades ago. The labor force participation rate has increased during this period in all of the countries studied by the Bureau of Labor Statistics, except Japan. In 2009, only a few countries, notably Canada and Sweden, had labor force participation rates for women that were higher than the U.S. rate.[29]

Women now "own 40 percent of all businesses and hold 43% of executive, administrative and managerial positions in the U.S. economy, narrowing the male-female wage gap to its lowest point in history."[30] Women have held over half of all managerial and professional specialty positions in 2013. Of members of boards of directors, 16.6% are women, and 8.1% of top earners are women. Meanwhile, 4.2% of Fortune 500 CEOs were women, and 14.3% of Fortune 500 corporate officers were women.[31] The Families and Work Institute also noted, in their National Study of the Changing Workforce, that "the desire for jobs with more responsibility among young women with children is at its highest point." Women have also made educational advances.

Figure 7.1

Does Your Organization Capitalize on Gender Strength?

- What evidence demonstrates that women enjoy working in the organization, and how is this monitored?
- What training and development opportunities are there, and how well are these accessed?
- What mentoring and coaching opportunities exist for women? How are these implemented and monitored?
- Do women have real choices about work–life responsibilities?
- How is women's advancement supported through internal networks?
- Who are the women's visible role models in the organization and why?
- How does the organization actively attract and position itself with women?
- What do the stats and trends show when it comes to attracting, retaining and developing women?
- How can women be assured of fair and transparent promotion processes, and accessible dispute mechanisms?
- How are equal pay for equal work, fair rewards, and recognition for women monitored?
- What do the women think about the effectiveness of parental and care support options?
- What external awards and recognitions have the organization (and the female employees) received?

Source: Adapted from Aurora Gender Capital Management's online service for women to research and compare organizations at http://www.wherewomenwanttowork.com.

It is projected that by 2016, women will "earn 60% of bachelor's, 63% of master's and 54% of doctorate and professional degrees."[32] Figure 7.1 suggests questions leaders and managers can ask to assess whether or not their organizations are capitalizing on gender diversity.

Catalyst released a survey discussing "Women in U.S. Corporate Leadership" in 2003 titled "What Keeps Women from Reaching the Top?"[33] The findings showed the top five barriers to be:

- Lack of significant general management or line experience (47%).
- Exclusion from informal networks (41%).
- Stereotyping and preconceptions of women's roles and abilities (33%).
- Failure of senior leadership to assume accountability for women's advancement (29%).
- Commitment to personal/family responsibilities (26%).[34]

In the same study participants cited the following top five success strategies they used to reach the top:

- Exceeding performance expectations (69%).
- Successfully managing others (49%).
- Developing a style with which male managers are comfortable (47%).
- Having recognized expertise in a specific content area (46%).
- Taking on difficult or highly visible assignments (40%).

Do you agree with the top five barriers women face to "get to the top" of organizations? If not, what factors do you believe account for the lack of advancement of women to more senior level and corporate board positions?

Same-Sex Marriages, Civil Unions, Domestic Partnerships, and Workforce Rights

The U.S. Supreme Court ruled on June 26, 2013 that section 3 of the Defense of Marriage Act is unconstitutional.[35] The federal government can no longer discriminate against married lesbian and gay couples with regard to federal benefits and protections.[36] Same-sex couples validly married by December 31, 2013 can file 2013 federal taxes as married couples.[37] Other tax changes were also amended under this law.[38]

In 2004, Massachusetts became the first state to grant gays and lesbians the right to marry. Whether or not other states will recognize Massachusetts' same-sex unions is unresolved. How would the benefits be affected, for example, of a same-sex married Boston employee moved by an employer to another state that prohibits gay marriages? "Civil union," a new legal category, has been created that extends rights to same-sex couples. At the time of writing, 13 states (Massachusetts, New Hampshire, Vermont, California, Connecticut, Iowa, Delaware, Minnesota, New York, Rhode Island, Maine, Maryland), plus the District of Columbia, allow same-sex marriage, and 35 states have limitations on it.[39] Marriage licenses are now issued to same-sex couples in Massachusetts, Connecticut, Iowa, Vermont, New Hampshire, New York, and the District of Columbia. New York and Maryland are the only states, to date, that recognize same-sex marriages from other states. Civil unions, as mentioned above, provide state-level spousal rights and are allowed in the following states: Delaware, Hawaii, Illinois, New Jersey, and Rhode Island. "Domestic partnership," another new category, was created that gives rights to unmarried couples, "including (but not necessarily limited to) same-sex couples. Laws vary among states, cities, and counties. Terminology also varies; for example, Hawaii has "reciprocal beneficiaries law." Domestic partnerships granting nearly all state-level spousal rights are allowed in California, Oregon, Nevada, and Washington. Those providing only some state-level spousal rights are Hawaii, Maine, Wisconsin, and the District of Columbia. These rights are recognized only on the state or local level so designated.[40]

Similar domestic partnership systems exist across the globe. Same-sex marriage is now legal in all Canadian provinces. Sweden legalized same-sex marriage in 2009, following Norway in 2008. The Netherlands expanded its definition of marriage in 2001 to include both opposite-sex and same-sex couples. Belgium followed in 2003, and same-sex couples have been allowed to adopt children since 2006. Spain also voted to extend full marriage rights to same-sex couples in 2005. Portugal and Iceland legalized same-sex marriage in 2010,[41] and Denmark followed in June 2012.[42] Most recently, New Zealand and France legalized it in 2013.

Some political jurisdictions have special legislation that allows gay and lesbian couples to register their committed relationships and gain some benefits. However, they do not receive all of the advantages that opposite-gender couples automatically acquire when they marry. These areas include most of the Scandinavian nations, states in the United States where the arrangement is called a civil union, and others.[43]

Several states have also expanded the legal rights available to spouses in same-sex relationships, while also limiting marriage to opposite-sex couples with civil unions and domestic partnerships. Six states have adopted civil unions available to both same-sex and opposite-sex couples. Civil unions provide legal recognition of the couples' relationship, while providing legal rights to the partners, similar to those accorded to spouses in marriages. From July 1, 2013, civil unions ceased to be offered in Delaware, and Rhode Island followed a month later, after the states' respective same-sex marriage laws took effect. Two states have adopted broad domestic partnerships that grant nearly all state-level spousal rights to unmarried couples. Domestic partnerships are available to both same-sex and opposite-sex couples.[44]

"At least 9,390 employers in the U.S. offer domestic partner health benefits for their employees. Of these, 95% offer the benefits to both same-sex and different-sex partners." According to the Bureau of Labor Statistics, only "thirty-three percent of state and local government workers and 29 percent of private sector workers have access to health care benefits for unmarried domestic partners of the same sex." A 2012 study showed that "51 percent of small businesses currently offer equal benefits to employees with same-sex partners or spouses, and 50 percent of those who do not say they would like to offer such benefits in the future."[45]

The Increasing Cultural Mix: Minorities Are Becoming the Majority

By 2050, the U.S. population is expected to increase from 282.1 million to 439 million. By as early as 2042, white people will be a minority in the United States. According to new projections from the Census Bureau, "ethnic and racial minorities will comprise a majority of the population of the United States in a little more than a generation." Minorities including Hispanics, Blacks, Asians, American Indians, and Native Hawaiians and Pacific Islanders "will together outnumber non-Hispanic whites." African Americans, Asian Pacific Islanders, and Hispanics made up more than one-third of the U.S. population in 2010 and the numbers have only continued to rise. By 2050, minorities will represent 54% of America.[46] The Hispanic community is one of the greatest untapped markets we have ever seen. Already the largest minority in the United States, their numbers continue to grow faster than any other group. Between 2000 and 2010, the Hispanic population grew by 43%, or four times the nation's 9.7% growth rate. In real numbers, this was an increase of 15.2 million people of Hispanic descent and accounted for more than half of the total U.S. population increase of 27.3 million.

The total population of Hispanics in the United States today is 50.5 million people strong. Hispanics are also one of the most optimistic groups: most believe the struggling economy has hit them the hardest, yet conversely, they have the highest hopes for the future. According to a Pew Hispanic Research survey conducted in January 2012, two-thirds of Hispanics expected to improve their financial status in 2012, while in the general population just over half said the same.[47]

Factors affecting this trend are birthrates and immigration.[48] Immigration undeniably benefits the United States; the economic advantages are significant. Many immigrants are natural entrepreneurs, establishing companies, creating jobs, and driving innovation. Well-educated and highly trained foreign workers are inventive and productive. Expanded workforces increase business flexibility, allowing companies to quickly respond to changing demands. Larger labor forces also encourage specialization. Labor productivity rises as companies adjust to larger work forces and invest in employees.[49]

It is projected that minorities "will constitute a majority of American children under 18 by 2023 and of working-age Americans by 2039."[50] This forecast indicates that by 2050, "the number of Hispanic people will nearly triple, to 133 million from 47 million, to account for 30 percent of Americans." The Asian population is expected to increase to 41 million, or more than 9% of the U.S. population; and the black population will increase to 66 million, or 15% of the population over the same period. "Several states, including California and Texas, have already reached the point where members of minorities are the majority." About 353 of the nation's 3,143 counties, or 11%, are now "majority-minority." Six of those counties tipped to that status in 2012: Mecklenburg, North Carolina; Cherokee, Oklahoma; Texas, Oklahoma; Bell, Texas; Hockley, Texas; and Terrell, Texas.[51]

For the first time in more than a century, the number of deaths now exceeds births among white Americans.[52] The aging white population has a significant impact on the trend toward diversity. "When all the baby boomers will have turned 65, nearly 20 percent of Americans will be over 65. The government also projects that in five years, minorities will make up more than half of children under 18. Not long after, the total U.S. white population will begin an inexorable decline in absolute numbers, due to aging baby boomers."[53] By 2050, about 89 million Americans will be in that group.[54] The impact of these demographic changes on markets, customers, workforce composition, values, and ethics will be significant.

Educational Weaknesses and Gaps

A recent global study on educational levels revealed several trends that will have a significant impact on the workforce, not only in the United States, but on a global scale. "Globally, the number of children enrolled at the secondary level has tripled since 1970."[55] In addition, "95% of primary school graduates continue their education at the lower secondary level in most countries in Central and Eastern Europe, Central Asia, and North America and Western

Europe." The education of those entering the workforce is now being shaped heavily by globalization, which is characterized by the dominance of English "as the dominant language of scientific communication"; the availability of "universal means of instantaneous contact and simplified scientific communication," and the "concentrated ownership of publishers, databases, and other key resources." This has created an "inequality among national higher education systems as well as within countries." Countries in Africa, for example, are not positioned with the same resources and educational standing. China and India, on the other hand, are "currently the world's largest and third largest academic systems."

These educational trends and gaps affect the pool of applicants and current employees. For example, it is projected that the majority of the student population in the most developed countries will be comprised of women. It is also expected that "the mix of the student population will become more varied, with greater numbers of international students, older students, part-time students, and other types."[56] This diversity has already begun to be reflected in the U.S. workforce.

A 2012 McKinsey & Co. report titled *Education to Employment* demonstrated the challenging mismatch between our educational system and the job skills employers need:[57] 45% of U.S. employers reported that lack of skills is the "main reason" for entry-level vacancies and only 42% of worldwide employers believe new graduates are adequately prepared for work.[58]

Interestingly, the United States shows no gap in education attainment, with very high levels of literacy and women's enrollment in primary, secondary, and tertiary education.[59]

POINT/COUNTERPOINT

Student Education Debt and Loans: Whose Problem and Who Should Pay?

Student loans exceed $1 trillion, which represents 81% of the most burdened borrowers. Those with over $40,000 of student debt have private loans with interest rates of or exceeding 8% or higher, according to the Consumer Financial Protection Bureau (CFPB). A College Board study stated that 60% of students who earned bachelor's degrees in 2012 graduated with debt. The average debt was $26,500.

The U.S. Congress has approved new rates for federal loans allowing undergraduates to borrow at a 3.9% interest rate for subsidized and unsubsidized loans. Graduate students will be able to borrow at 5.4%, and parents can borrow at 6.4%, at least for 2013.

Unlike federal student loans, private loans cost more because they offer less repayment flexibility and typically cannot be discharged in bankruptcy. Most student debt is difficult, almost impossible, to refinance—burdening borrowers with high rates in a low-rate environment and slowing the economy. "Repaying a student loan should be simple," CFPB director Richard Cordray said in a statement. "When servicers process payments to maximize fees and

penalties they undermine the trust of their customers. Student loan borrowers deserve better; they deserve transparency and accountability."

Nearly half of all complaints were related to struggling borrowers who were seeking a loan modification or other option to reduce their monthly payment.

The average American will also likely see interest rates increase as the Treasury increases rates to attract investors. Interest rates will also increase for mortgages, car loans, student loans, and credit cards. The cost of higher education is also creating a sense of more burden than benefit for some students. A Wells Fargo study found that one-third of Millennials said they would have been better off working instead of going to college because of having to pay tuition.

Rising costs in education increases student loan debt. An art degree costs as much as a computer science degree. Which is more likely to result in a job? Lenders, in this case the government, should make a fact-based determination of a student's likelihood to graduate and get a job, and their expected income. Prospective students applying for loans could be evaluated for "credit worthiness" score. A student loan score would be based on a formula including their grade point average, major, and academic institution. Each of these variables is directly related to a student's ability to get a job upon graduation and repay their loans. For example, a STEM (science, technology, engineering and mathematics) major at MIT would yield a higher score and loan compared to a religious studies major at a lesser-ranked school.

Instructions: (1) Each student individually will adopt *either* the Point *or* CounterPoint argument and justify their reasons (with arguments using this case and other evidence/opinions). (2) Then, either in teams or designated arrangements, each shares their reasons. (3) Class debrief and sharing of insights.

POINT: Students should pay their debts; they borrowed, they pay. What precedent does this set in a capitalist, market economy? It's time to stop treating all degrees alike. Some degrees result in jobs, others don't. Create a scoring system and even backdate it. Those degrees that have high job potential should have different payback terms than those that don't. If the loans are not paid, the economy continues to suffer and we all pay. Next, people will want the government to pay for their mortgages, car loans, and then what?

COUNTERPOINT: The government should forgive and absorb student loan debts. The loans and terms made were and are unstable and are near impossible to collect from every student. Students are assets to the future of this country. Why treat them like their loans—liabilities? Education is the foundation of democracy. Should students be encouraged to become hourly wage workers at low-tech jobs? Learning how to think creates good citizens, a middle class, and entrepreneurs—and their degrees don't have to be only in computer science.

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Mainstreaming Disabled Workers

Hiring and mainstreaming qualified disabled workers is increasing in importance because of the combined effects of the shrinking and aging of the workforce. The International Labor Organization estimated that 386 million working-age people globally have a disability, and that "unemployment among persons with disabilities is as high as 80 percent in some countries."[60] Disabilities affect a large percentage of the workforce. In 2004, only 35% of working-age people with disabilities in the United States were employed. "One third of the employers surveyed said that persons with disabilities cannot effectively perform the required job tasks. The second most common reason given for not hiring persons with disabilities was the fear of costly special facilities." Disabilities are categorized as permanent (for example, physical disabilities), temporary (such as those resulting from injury or stress), and progressive (e.g., AIDS, alcohol and drug addiction, cancer). An assessment from the National Organization on Disability/Harris Survey of Americans with Disabilities concluded that disabled Americans are three times as likely to live in poverty as the general public, twice as likely to drop out of

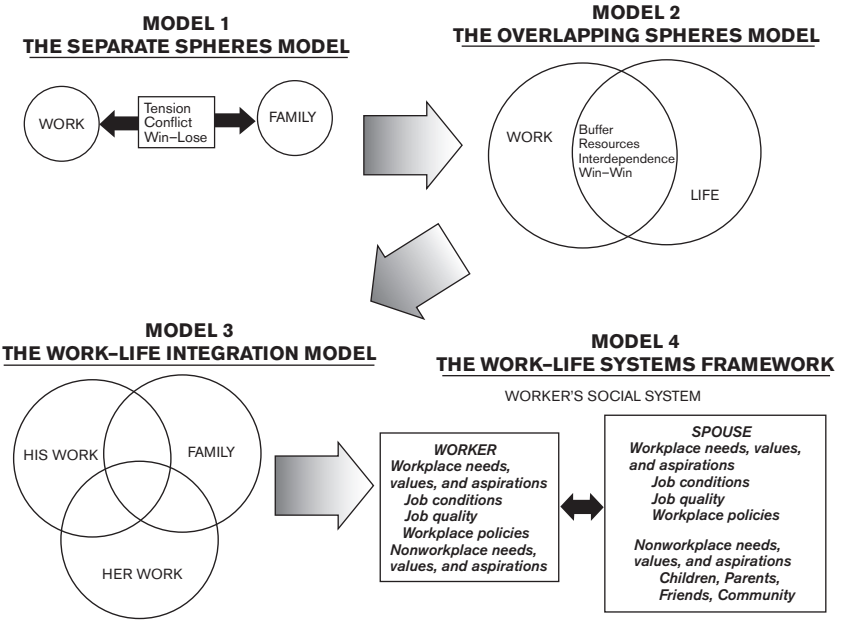
high school, and twice as likely to be constrained by transportation options; also, three times as many individuals with disabilities have less health care than the general public. It is interesting to note that "everybody is just one car wreck away, a diagnosis away, a progressive condition away from joining the ranks of the disabled."[61] Employers who hire persons with disabilities report they are more likely to be loyal, appreciative to their employers, and able to think outside the box.

Balancing Work and Life in Families

As more dual-career and child-rearing couples enter the workforce, conflicts and problems evolve over roles and responsibilities as families cope with workplace demands. Working family models illustrating these tensions have evolved over decades. Four such models, which are summarized in Figure 7.2, include (1) an early model depicting complete separation of work and family life and issues, in which men worked and women maintained the family; (2) an overlapping model of "work" and "family life" spheres in which the boundaries were still fuzzy, but roles were recognized as being interrelated; (3) a model that defined multiple roles and responsibilities, including "his work," "her

Figure 7.2

Evolution of Work and Family Life Systems Models



Source: Adapted with permission from Barnett, R. (March 1999). A new work–life model for the twenty-first century. *Annals of the American Academy of Political and Social Science, 562,* 143–158.

work," and "family" obligations, which, like the previous two models, was based on scarcity and zero-sum assumptions (i.e., a fixed number of resources that resulted in win–lose situations) regarding the allocation and use of resources and responsibilities at home and at work; and (4) the most recent work–life systems model, which assumes a systems perspective in which roles and responsibilities are not seen as competitive, isolated, or overlapping in undefined ways between family members, and the organization and community are built into individual and family responsibilities, which are shared to optimize the well-being of the entire system (company, employees, and families). In the fourth model, the emphasis also shifts from individual and family to include workplace needs, values, and aspirations; job conditions; and quality of life. Company policies are recognized as part of the work–life equation and include flextime and part-time arrangements.

Several companies have consistently been ranked among the top 10 firms over the past five years from the annual survey of the "100 Best Corporations for Working Mothers." These companies include Deloitte, Discovery Communications, Ernst & Young, General Mills, PricewaterhouseCoopers, WellStar Health System, and Bank of America.[62]

In the following sections, we turn to topics regarding how employers have dealt with, and are dealing with, the legal and ethical issues of changing workforces.

7.2 The Changing Social Contract between Corporations and Employees

The social contract that has historically defined the employee–employer relationship is known as the "employment-at-will (EAW) doctrine." Basically, the EAW doctrine holds that the employer can dismiss an employee at any time for any reason, as long as federal and state laws and union contracts are not violated; likewise, employees are also free to terminate their employment with a company whenever they choose and for whatever reason. This doctrine remains the dominant view of the employment relationship in the United States, although parts of the doctrine have eroded since its inception.[63] The EAW doctrine has been in effect since 1884, when the *Payne v. Western & Atlantic R.R. Co.* judgment ruled that "all may dismiss their employees at will, be they many or few, for good cause, for no cause, or even for cause morally wrong without being thereby guilty of legal wrong." Essentially, the EAW doctrine can be defined as "the right of an employer to fire an employee without giving a reason and the right of an employee to quit when he or she chooses."[64] If employees are unprotected by unions or other written contracts, they can be fired, according to this doctrine. As the insert "Read Carefully before Signing" shown in Figure 7.3 illustrates, employees can be and are asked to acknowledge how tenuous their "contract" with a company can be.

The EAW doctrine evolved as part of the laissez-faire philosophy of the Industrial Revolution. Between the 1930s and 1960s, however, excep-

Figure 7.3

Employee Contract under the EAW Doctrine

Read Carefully before Signing

I understand that refusal to submit to the testing noted [elsewhere] or a positive drug screen result will eliminate any consideration for employment.

I also certify that the statements and information furnished by me in this application are true and correct. I understand that falsification of such statements and information is grounds for dismissal at any time the company becomes aware of the falsified notification. In consideration of my employment, I agree to conform to the rules and regulations of the company and acknowledge that my employment and compensation can be terminated, with or without cause, and with or without notice, at any time, at the option of either the company or myself. I further understand that no policy, benefit or procedure contained in any employee handbook creates an employment contract for any period of time and no terms or conditions of employment contrary to the foregoing should be relied upon, except for those made in writing by a designated officer of the Company.

I agree and hereby authorize XYZ, Inc. to conduct a background inquiry to verify the information on this application, other documentation that I have provided and other areas that may include prior employment, consumer credit, criminal convictions, motor vehicle and other reports. These reports may include information as to my character, work habits, performance, education and experience along with reasons for termination of employment from previous employers. Further, I understand that you may be requesting information from various federal, state and other agencies which maintain records concerning my past activities relating to my driving, credit, criminal, civil, and other experiences, as well as claims involving me in the files of insurance companies. I authorize all previous employers or other persons who have knowledge of me, or my records, to release such information to XYZ, Inc. I hereby release any party or agency and XYZ, Inc. from all claims or liabilities, whatever that may arise by such disclosures or such investigation.

_____ _____

Date of Application Signature of Applicant

tions to the doctrine appeared. Federal legislation since the 1960s has been enacted to protect employees against racial discrimination and to provide rights to a minimum wage, to equal hiring and employment opportunities, and to participation in labor unions. Over time, the following exceptions to the EAW doctrine have evolved: (1) the good faith principle; (2) the public policy principle; and (3) implied contracts.

Good Faith Principle Exception

Some states have other obligations that must be addressed by employers, like "good faith" or "fair dealing" practices.[65] A good faith principle is based on the premise that employers should practice fairness and reasonableness in their actions with employees. For example, an employer should demonstrate that opportunities were offered for a terminated employee to improve his/her performance before the employee was fired. Companies that demonstrate fairness in their dealings and policies with employees show good faith.[66]

Public Policy Principle Exception

Since the 1970s, state court decisions have limited the EAW doctrine. Specifically, state courts have upheld employees' rights to use legal action against their employers if an employee termination violated "public policy" principles; examples include (1) if employees were pressured to commit perjury or fix prices; (2) if employees were not permitted to perform jury duty or file for workers' compensation; (3) if employees were terminated because they refused to support a merger; and (4) if employees reported alleged employer violations of statutory policy (whistle-blowing).[67]

Implied Contract Exception

An important 1981 California Appeals Court decision, *Pugh v. See's Candies, Inc.,* ruled that, in a noncontractual employment arrangement, an implied promise from the employer existed. The employer could not act arbitrarily with its employees regarding termination decisions when considering the following factors: (1) duration of employment; (2) recommendations and promotions received; (3) lack of direct criticism of work; (4) assurances given; and (5) the employer's acknowledged policies.[68] Other implied contract exceptions include statements in employee and personnel handbooks, manuals, guidelines, letters offering employment, and verbal statements made to employees regarding job security and promises of continuing employment.[69]

Although the EAW doctrine has undergone change, it remains the cornerstone of U.S. labor law, as is illustrated in Figure 7.3. States vary on the application of the EAW doctrine, but the U.S. Eighth Circuit Court of Appeals favored employers. The federal court has stated that it will not act as a "superpersonnel board" of a company. Figure 7.3 is a copy of a contract an employee must sign before beginning work at this reputable company in Massachusetts. It is an example of a strongly worded EAW-oriented contract.

At issue in the EAW doctrine is the continuing debate over the nature of property and property rights. Each organization defines property rights and responsibilities offered to managers and employees, such as severance payments, pensions, stock options, access to resources, and golden parachutes. Employers also view employees' labor, time, and effort as part of their property. At issue in the EAW doctrine is whether an employee's education, skills, and other intangible assets are seen as the employee's "property," and if so, whether employees have certain rights regarding these assets. Due process is one such right that accompanies the EAW doctrine.[70]

The debate will continue over whose "property" and rights take precedence, and whose are violated and on what grounds, between employer and employee, especially in disputed firings that do not involve clear legal violations of employee rights, such as blatant discrimination. One scholar has noted that "The present-day debate revolves mainly around utilitarian issues. To what extent is the welfare of society advanced by preserving or limiting the traditional prerogatives of employers? Employers typically favor employment at will not because they want to fire without cause but because they

would rather avoid the need to account for their personnel decisions in court and face the possibility of stiff punitive awards. Even advocates of greater employee protection recognize the dangers of the courts becoming too deeply involved in business decision making."[71]

The next section presents employee rights and employer responsibilities and offers recommendations to managers for avoiding arbitrary termination decisions.

7.3 Employee and Employer Rights and Responsibilities

Employers and employees have rights and responsibilities each should honor with respect to the other. This section discusses these mutual responsibilities, some of which stem from rights by law and legislation, while others are based on ethical principles. As discussed in Chapter 5, a values-based, stakeholder management approach views the employer–employee relationship as one grounded on mutual trust and reciprocal responsibility. Although laws and legislation serve the purpose of protection for both parties, without trust that is demonstrated in fair and equitable treatment of basic rights and responsibilities, one or both parties stand to lose. Nevertheless, not all employers or employees have a personal, professional, or organizational ethic that respects the other's rights in all situations. Historical attitudes, negative prejudices, and stereotypes sometimes surface in institutionally unjust practices toward individuals and groups. On the other hand, employers must protect their property and assets against illegal and unethical practices of certain employees. When voluntary trust and mutual respect fail and harm is done to employers or employees, the legal system can be evoked.

The EAW doctrine was a transition from a feudal European governance context to a modern pluralistic U.S. context. Employers still control private property and proprietary rights over their intellectual property. Employees claim their constitutional rights to individual freedom, liberty, and control over their private lives. Employers try to maximize productivity and profits, to sustain financial growth and stability, to minimize costs, to improve quality, to increase market share, and to stabilize wages. Employees seek to increase their wages and benefits, to improve working conditions, to enhance mobility, and to ensure job security while demonstrating mutual respect for the value of their labor. No perfect boundary exists between employer and employee rights in a capitalist market economy.

Before discussing specific rights and responsibilities between employers and employees, this section begins by defining "rights" and two premises based on this definition. Then, two organizing concepts that underlie employee rights are suggested: balance and governmental rights. The concept of balance is based on utilitarian ethical reasoning and that of moral entitlement is based on Kantian nonconsequentialist reasoning. Although these concepts are not mutually exclusive, it is helpful to understand the logic behind them in order to argue their merits and shortcomings as they apply to specific workplace controversies.

Moral Foundation of Employee Rights

The ideal relationship between employer and employees is one based on mutual respect and trust. Trust generally leads to open communication, which, in turn, provides an environment of collaboration and productivity. In many companies, this is, unfortunately, not the case. Power and authority relationships between employers and employees are, by definition, asymmetrical. Employees are generally, as stated by J. Rowan, in a "comparatively inferior bargaining position with respect to their employers. This inequity opens up possibilities for various sorts of exploitation, such as inadequate compensation, discrimination, and privacy invasions, all of which have been known to occur." Rowan also notes that "employee rights are complex, in that managers, as a prerequisite for making ethically sound decisions, must assess which alleged employee rights are legitimate . . . and must weigh them against the rights of those in other stakeholder groups."[72]

A right can be understood as a "moral claim." A right is moral when it is not necessarily part of any conventional system, as are legal rights. A right is a claim because it corresponds with a duty on the part of the person against whom the right is held. For example, I claim that I have a right to be safe in my workplace. I hold this claim against my employer, because the employer has the duty to provide me with this safety. Under particular circumstances, my moral claim can be argued and disputed. It may not be an absolute claim.

The moral foundation for employee rights is based on the fact that employees are persons. One generic right that all persons have is a right to freedom, including the concept of negative freedom (i.e., the right not to be coerced or inhibited by external forces). Regarding employees, this right to freedom is a claim "that when managers choose to hire employees, they must bear in mind that they are dealing with persons, and the (positive and negative) freedom of their employees is therefore to be respected."[73] The second generic right of employees is the right to well-being. This right follows from individuals' having interests, which are preconditions for pursuing goals. Interests and the pursuit of goals are morally important because they are not satisfied when a person does not have well-being. When employees cannot satisfy their job-related goals, interests, and requirements because of work-related conditions, an employee's right to well-being may have been violated. With regard to these arguments on the moral foundation of employee rights, Sanford Jacoby has noted, "Employees should at all times be treated in a way that respects them as persons."[74] We might add that the same observation holds true for employers; they also should be treated with respect as individuals.

The Principle of Balance in the Employee and Employer Social Contract and the Reality of Competitive Change

As common law and custom have evolved from the EAW doctrine to implied employee rights, employers have the opportunity to consider more than stockholder and financial interests when dealing with employee stakeholders.

As discussed in Chapter 5, a values-based stakeholder management perspective views the employee–employer relationship from a win–win foundation. Both employers and employees act from a base of values. Employer-employee working relationships are enhanced when the values of the organization reflect and align stakeholder with stockholder interests. Productivity, innovation, personal and professional growth are more likely to result from this type of alignment.

In a highly competitive, globalizing environment in which intellectual skills, flexibility, and speed of work are emphasized, traditional views of company ownership and employee loyalty change. Employees' and workers' needs can also be diminished in polarizing political climates where governmental bodies and coalitions funded by interest groups seek to implement special demands. The evolving social contract between employers and employees still recognizes employers' power over their physical and material property, but the contractual relationship between employer and employee aims in principle at balance, mutual respect, integrity, and fairness. The employer's business interest can and should be balanced against the employee's welfare, interests, and willing contribution to add value. In the early twenty-first century, small- and mid-sized employers are also pressured to balance global economic demands and tighter profit margins with employee interests. Larger firms continue to reduce their workforce and cut costs through outsourcing and offshoring, as discussed earlier in the text. Although employers generally have more power than employees in the contractual relationship, employees in the United States, for example, are still citizens under the protection of the Constitution. Employees must also balance their self-interests and motivations with the need of the organization to succeed, which is necessary for the organization to provide employment.

It is interesting to note that the principle of balance in the employer–employee relationship has been historically prevalent in some of the developed Asian countries, such as Japan, South Korea, Singapore, and Taiwan. In Japan, in particular, the Confucian tradition of harmony has underscored the cooperative relationship between unions and companies.[75] European countries, including Germany and France, have also enacted laws that protect employee benefits and welfare. Some of these countries have traditions that include socialism and strong populist social policies. Some of these traditions and practices are also beginning to change under the competitive pressures of economic downturns, the use of information technology, and global competition. For example, lifelong employment in many Japanese companies is no longer guaranteed. Offshoring and outsourcing are now practiced at Sony, Matsushita, and Toshiba, to mention just a few firms.[76]

Rights from Government Legislation

Employee rights are based on principles determined by law. Certain government rights (federal, state, and local) of the employee are not negotiable in written or implied contracts, for example, rights related to the minimum wage; sexual harassment; discrimination based on race, creed, age, national

origin, gender, or disability; and the right to assemble. Although employee rights based on certain legislation are not always negotiated according to employer–employee self-interests, these rights can be disputed, depending on circumstances. Reverse discrimination, to be discussed later, is one such example. Although private corporations are the property of the owners, certain employee legal rights are still within a corporation's boundaries. (Refer back to Chapter 2 for a discussion of different classifications of moral rights.)

Employer Responsibilities to Employees

Employers are obliged to pay employees fair wages for work performed and to provide safe working conditions. Review and answer the questions in the box entitled, "Who Has Rights in this Situation?" After you have answered and discussed the questions, what, if anything, did you learn about your and other classmates' values and beliefs regarding employee–employer responsibilities, obligations, and rights?

Fair Wages

Fair wages are determined by factors such as what the public and society support and expect, conditions of the labor market, competitive industry wages in the specific location, the firm's profitability, the nature of the job and work, laws governing minimum wages, comparable salaries, and the fairness of the salary or wage negotiations.[77] As we will see later in this chapter, fair wages for comparable jobs held by men and women are not always paid.

Full-time working women had median weekly earnings of $713, or 82% of the $869 median for men. Full-time working black men earned a median weekly wage of $646 per week, or 72.1% of the median for white men ($896). Full-time working black women earned a median weekly wage of $621, or 85.3% of those for white women ($728). Median earnings of full-time employed Hispanics was $576—lower than those of blacks ($632), whites ($813), and Asians ($916).[78]

Based on The Institute for Women's Policy Research wage gap fact sheet, "If the pace of change in the annual earnings ratio continues at the same rate as it has since 1960, it will take another 45 years, until 2058, for men and women to reach parity."[79]

Who Has Rights in This Situation?

Aparna Jairam (a high-tech employee in India) isn't trying to steal your job (you're a high-tech U.S. employee). That's what she tells me, and I believe her. But if Jairam does end up taking it—and, let's face facts, she could do your $70,000-a-year (U.S.) job for the wages of a Taco Bell counter-jockey—

she won't lose any sleep over your plight. When I ask what her advice is for a beleaguered American programmer afraid of being pulled under by the global tide that she represents, Jairam takes the high road, neither dismissing the concern nor offering soothing happy talk. Instead, she recites a portion of the 2,000-year-old epic poem and Hindu holy book, the Bhagavad Gita: "Do what you're supposed to do. And don't worry about the fruits. They'll come on their own."

QUESTIONS

1. Do you agree with Aparna? Why or why not? Please explain.
2. On what, if any, ethical grounds could you either justify or reject her assessment? Explain.

SOURCE

Pink, D. (February 2004). The new face of the silicon age. *Wired Magazine, 12(2).* http://www.wired.com/wired/archive/12.02/india.html, accessed January 8, 2014.

Safe Working Environment

Employers also are obliged to provide workers with a safe working environment and safe working conditions. The Occupational Safety and Health Administration (OSHA) and federal laws and regulations provide safety standards and enforce employer institution of the company's own safety standards. The problems of employers providing—and of employees accepting—safe working environments stem from: (1) lack of knowledge and of available, reliable information about levels of health risks; (2) lack of appropriate compensation proportional to the level of occupational risk; and (3) employees accepting known risks when the employer does not offer any safer alternatives. When the option is employment versus no employment, workers, especially in low-income, noncompetitive employment regions, often choose jobs with hazardous risks to their health or life. Employees have a right to know about unsafe working conditions, as we also discuss later in the chapter.

Employers should pay competitive wages commensurate with the occupational risks associated with a profession, job, or work setting. For example, race car drivers would not be expected to receive the same pay as college professors. Employers also are expected to provide full information on the risks and health hazards related to the work, products, and working environments to all employees exposed to those risks. Finally, employers also should offer health insurance programs and benefits to employees exposed to workplace hazards. Not all employers, especially with recent economic conditions, meet these obligations. Employers who cannot provide health and protection

of employees in high risk, potentially unsafe environments should not be in that business.

Many companies are proactive in developing standards and monitoring for safe working conditions. Apple, for example, announced in February 2012 that it would audit the working conditions at its overseas factories and make the findings public, through the Fair Labor Association. The company has made a public commitment to hold its supply chain accountable for appropriate, safe working conditions. "Apple has said that if the companies manufacturing its products do not measure up to its labor and human rights standards, it will stop working with them." Apple, like many manufacturers, has not been immune to incidents with unsafe working conditions. Company reports indicate previous instances of "excessive overtime, underage workers, improperly disposed hazardous waste and falsified records." In 2010, "137 workers at an Apple supplier in eastern China were injured after they were ordered to use a poisonous chemical to clean iPhone screens." In 2011, "two explosions at iPad factories killed four people and injured 77." It is expected that there will be repercussions across the electronics industry, as Apple is an industry leader and many of the suppliers are used by multiple companies within the industry. Apple was the "first technology company to join the Fair Labor Association," joining in January of 2012.[80]

Working Conditions that Empower Employees

Although employers are not required by law to offer employees working conditions that provide meaningful tasks and job satisfaction, doing so can lead to increased performance, job satisfaction, and productivity. Employees work most productively when they can participate in the control of their tasks, when they are given responsibility for and autonomy over their assignments, and when they are treated with respect.[81] Quality of work life (QWL) programs that have provided employees with more autonomy, participation, satisfaction, and control in their work tasks have demonstrated positive results.[82] Many companies that have organized self-designing work teams, quality circles, and learning communities to tap into employee creativity and abilities have also provided opportunities for innovation. As noted in Chapter 5, there is an increase in companies offering opportunities for employees to practice their own religious and spiritual rituals during the work day. Employers and employees both gain when personal and organizational needs are met. Working environments that can provide conditions for this alignment are increasing in order to attract and retain talent.

Employee Rights and Responsibilities to Employers

Employees are responsible for fulfilling their contracted obligations to the corporation; for following the goals, procedural rules, and work plans of the organization; for offering competence commensurate with the work and job assignments; and for performing productively according to the required tasks. Other responsibilities include timeliness, avoiding absenteeism, acting legally and morally in the workplace and while on job assignments, and respecting the intellectual and private property rights of the employer.

Employee Rights in the Workplace

Labor, along with money and materials, is considered capital in a free-market system. However, labor is not the same as materials and money; labor also means human beings who have general constitutional rights that should not be relinquished between working hours.[83] Yet, clashes of interests and of stakes between employee rights and management demands frequently occur. The boundary between an employer's private property and an employee's individual rights is often blurred in everyday experience. Understanding employee rights is part legal and part ethical because these rights must be viewed and interpreted within corporate policy, procedures, and particular circumstances. In some instances, there are clear violations of an employee's rights; other times there are "gray," or uncertain, areas. When employees and employers cannot agree on whose rights are seriously violated, third-party negotiation, arbitration, and even settlement may be required. This section presents major types of employee rights in the workplace:

- The right not to be terminated without just cause.
- The right to due process.
- The right to privacy.
- The right to know.
- The right to workplace health and safety.
- The right to organize and strike.
- Rights regarding plant closings.

These rights become even more important in a society that rapidly transforms technological and scientific inventions into part of the human workplace environment.

Just Cause Termination

A basic principle in disciplinary termination cases is that the employer must have "just cause" for imposing the action. A test for determining whether there is "just cause" was developed by Arbitrator Daugherty in the celebrated Enterprise Wire case (46 LA 359, 1966 and 50 LA 83). An absolute "no" answer to any one or more questions in this guideline indicates that the employer's action was "arbitrary, capricious and/or discriminatory in one or more respects, thereby signifying an abuse of managerial discretion and allowing the arbitrator to substitute his judgment for that of the employer."

1. Was the employee adequately warned of the consequences of his conduct?
2. Was the employer's rule or order reasonably related to efficient and safe operations?
3. Did management investigate before administering the discipline?
4. Was the investigation fair and objective?
5. Did the investigation produce substantial evidence or proof of guilt?
6. Were the rules, orders, and penalties applied evenhandedly and without discrimination to all employees?
7. Was the penalty reasonably related to the seriousness of the offense and the past record?[84]

As a principle, it also has been argued that workers should have three rights regarding work to maintain self-respect:

- The right to employment.
- The right to equal opportunity.
- The right to participate in job-related decisions.[85]

These rights are less entitlements than goals and depend on market conditions. Just cause termination is problematic when other forms of employer discrimination are determined, such as discrimination in age, gender, disability, race, national origin, and other Title VII areas. For example, an Ohio jury awarded a 68-year-old woman $30.6 million in an age discrimination lawsuit after a jury ruled that the company violated her rights by refusing to give her another job within the company when it terminated her from her management position.[86]

Due Process

Due process is one of the most important underlying rights employees have in the workplace because it affects most of their other rights. Due process refers to the right to have an impartial and fair hearing regarding employers' decisions, procedures, and rules that affect employees. As applied in the workplace, due process essentially refers to grievance procedures.

At a more general level, due process rights protect employees from arbitrary and illegitimate uses of power. These rights are based on the Fifth and Fourteenth Amendments of the Constitution, which state that no person shall be deprived of "life, liberty, or property, without the due process of law."

Patricia Werhane states that the following corporate procedural mechanisms are needed to ensure employees' right to due process:[87]

- Right to a public hearing.
- Right to have peer evaluations.
- Right to obtain external arbitration.
- Right to an open, mutually approved grievance procedure.

The right to due process applies to other employee rights, such as those involving privacy; safety and health; safe working environments; holding meetings and gatherings; and hiring, firing, and other human resource decisions.

Right to Privacy

Employees' right to privacy remains one of the most debated and controversial rights. It raises these questions: Where does the employer's control over employee behavior, space, time, and property begin and end? What freedoms and liberties do employees have with employer property rights? What rights do employers have to protect their private property, earnings, and costs from employees? The U.S. Constitution does not actually refer to a person's right to privacy; the working definition of employees' right to privacy has come to

mean "to be left alone." Privacy in the workplace also can refer to employees' right to autonomy and to determine "when, how, and to what extent information about them is communicated to others."[88] The extent of an employee's privacy in the workplace remains an unsettled area of controversy. The definition of what constitutes an employee's privacy is still somewhat problematic, including the notion of psychological privacy (involving an employee's inner life) and the notion of physical privacy (involving an employee's space and time).[89] In the 1965 *Griswold v. Connecticut* case, the Supreme Court ruled that the Constitution guarantees individuals a "zone of privacy" around them into which the government cannot intrude. Proponents of this definition argue that this zone includes personnel records and files and protection against polygraph and psychological testing and surveillance in the workplace. The ruling also is intended to protect employees in their after-work activities; their need for peace and quiet in the workplace; their dress, manners, and grooming; and their personal property in the workplace. Identifying this "zone of privacy" has proved complicated, especially in cyberspace and the use of technological surveillance.

Technology and Employee Privacy

Although employee privacy rights remain largely undefined regarding uses and abuses of emerging technologies in the workplace, the following main types of court-upheld privacy violations and permissible employee privacy inquiries can serve as guidelines. Court-upheld privacy violations include:

1. Intrusion (locker room and bathroom surveillance).
2. Publication of private matters.
3. Disclosure of medical records.
4. Appropriation of an employee's name for commercial uses.
5. Eavesdropping on employee conversations and retrieving or accessing employee e-mail (if unauthorized).

Permissible employee privacy inquiries include:

1. Criminal history inquiries.
2. Credit history inquiries.
3. Access to medical records.[90]

Conflicts of Interest

Employee responsibilities to employers become complicated when conflicts of interest appear; that is, when an employee's private interests compete or are not aligned with the company's interests. More obvious conflicts of interest arise in a number of situations, such as taking or offering commercial or personal bribes, kickbacks, gifts, and insider information for personal gain.

The so-called gray areas are more problematic for determining whose interests are violated at the expense of others. For example, an employee quits a firm, joins a competitor, and then is accused by the former employer of

stealing proprietary property (i.e., passing on intellectual property, sharing trade secrets, or offering a competitive advantage by divulging confidential information). Whose interests are violated?[91] Some courts have used a "balancing model" based on utilitarian logic to resolve trade-secret-protection cases; that is, an employee's interest in mobility and opportunity is weighed against the employer's right to decide the extent of protection given to confidential information. For example, the following three criteria have been used to decide whether trade secrets have been divulged by employees:

1. True trade secrecy and established ownership must be shown.
2. A trade secret must have been disclosed by an employee, thus breaching a duty of confidentiality.
3. The employer's interest in keeping the secret must outweigh the employee's interest in using the secret to earn a living and the public's interest in having the secret transmitted.

Courts also use other considerations in these types of rulings (for example, contract obligations, promises made, truthfulness, confidentiality, and loyalty). The point here is that as technology and expertise become more sophisticated and as employee mobility—and downsizing—increase, workplace and courtroom criteria regarding the proof of conflict of interest also grow more complicated. Although a utilitarian model is used to help determine conflict-of-interest court cases, such as trade secrecy, ethical principles such as rights, duty, and justice also remain essential considerations for determining right and wrong; violations of loyalty, confidentiality, or truthfulness; and harm done to either employers or employees.

Other Employee Rights and Obligations to Employers

Polygraph and Psychological Testing

Employers are particularly concerned about employee privacy rights regarding testing. Polygraph and psychological testing, and other related techniques that many managers would like to use to prevent and detect crime in the workplace, may constitute a violation of employee rights. Workplace theft has been estimated by the U.S. Department of Commerce to cost in excess of $40 billion a year in the United States.[92] Here are some of the issues surrounding the use of polygraphs and psychological testing:

1. These tests are not reliable or valid; they are only indicators.
2. The tests, to some extent, can be manipulated and influenced by the operators.
3. The tests may include irrelevant questions (such as those pertaining to gender, lifestyle, religion, and after-work activities) that invade a person's privacy.
4. Employees do not have control over the test results or how the information is used.

Researchers in the field of honesty testing have concluded that only 1.7% (at worst) to 13.6% (at best) of such tests are accurate.[93]

Workplace Surveillance

Surveillance of employees at work (that is, employers using technology to spy on and invade workers' privacy) is also a subject of concern. Software programs are used to monitor workers who use computer terminals.[94] Although there are pros and cons of surveillance videos in the workplace, as Ethical Insight 7.2 shows, there are no clear-cut answers as to whether or not to use such equipment to monitor employee performance. Employers can detect the speed of employees' work, number and length of phone calls made and received, breaks taken, when machines are in use, and so on. Although some form of work-related monitoring is certainly legal and even necessary, the ethical issues that the American Civil Liberties Union (ACLU) raise are the possible invasion of employee privacy and fair treatment. What type of information does an employer have a right to, and what effects do stress and anxiety from monitoring have on employee welfare? The Electronic Communications Privacy Act renders electronic eavesdropping through computer-to-computer transmissions, private videoconferences, and cellular phones illegal.

A study released by the Society for Human Resource Management, a trade association in Alexandria, Virginia, showed that 80% of the organizations in the study used e-mail. Only 36% of those groups had policies concerning e-mail use and only 32% had written privacy policies. The issue of individual employee privacy remains somewhat undefined in the workplace.[95]

Ethical Insight 7.2

Pros and Cons of Employers Using Video Surveillance

Pros	Cons
Increased safety: Improves the security of employers and employees.	*Potential invasion of privacy:* Camera installation in improper locations and video footage monitored and stored inappropriately presents liability for invasion of privacy claims and costly legal actions.
Theft deterrent: Saves companies by preventing stolen products.	*Can provide false sense of security.*
Prompts good behavior: Monitoring can encourage productive behavior.	*Lowers morale:* Can promote a lack of trust, negatively affecting an employee's work performance.
Provides evidence of a crime: Proof of stolen goods can be provided with electronic monitoring.	

Questions

1. How would electronic video surveillance affect you and your performance in the workplace?
2. Can you identify with an employer's need and justification for this equipment? Explain.

3. What other means of monitoring employee performance would you recommend and why?

Source: Bryant, Lynn. (October 12, 2006). What are the pros and cons of monitoring employees using video surveillance? http://www.video-surveillance-guide.com/monitoring-employees-using-video-surveillance.htm, accessed February 3, 2014.

Internet Use in the Workplace

This is another undefined area regarding employee use of technology that requires the employer's development of "appropriate use policies" (AUPs). The use of the Internet for personal reasons has become a significant source of wasted time and productivity loss for many companies. Social media is a particularly tricky culprit—many companies have turned to social media for advertising and communication among employees; however, the temptation and access to the Internet for personal reasons is great. "An April 2010 study by managed security services company Network Box shows employees visit Facebook on the job more than any other web site. Facebook usage is double that of the next most popular site, Google. A 2009 Deloitte LLP study showed nearly 40 percent of employees never take into consideration what their employers would think about their social media site postings."[96]

A poll taken by eMarketer in 2014 found that nine in ten U.S. companies will use social media for marketing purposes in 2014 to promote their branding. A growing number of companies also have social media policies in place for employees as well as for marketing and other operational purposes.[97] Such policies can help mitigate risks. Consider the following example: "let's say a manager at a Fortune 500 company posted a disparaging Facebook comment about one of his clients. His boss saw the comment and asked him to remove it, but it was too late. Someone forwarded the comment to the client, and the company lost a huge piece of business and took a serious blow to its reputation. The person who posted the comment also lost his job."[98]

Companies must find the appropriate balance of Internet use for personal and professional reasons, as the Internet (particularly social media) is such an integrated part of the lives of employees and can have many benefits to the company. AUPs are a good start.

Jo Tucker, head of labor and employment practices at Morrison and Foerster, a law firm based in Irvine, California, stated that "if a worker is using a computer in a company office, on company time, privacy is what the employer says it is."[99] Without AUPs, Internet use in the workplace remains a guessing game between employer and employee. An employee Internet use policy depends on the company, its corporate culture, and the nature of its business. The policy must have the involvement and endorsement of top-level leadership. Monitoring capability, with employee awareness, must also accompany the policy. As J. Martin states, "A clear AUP policy effectively removes employee expectations of privacy on the Internet, eliminating potential lawsuits."[100] All use policies should also be spelled out clearly with no ambiguities and with simple, easy, enforceable rules. Part of such a policy involves the

security of data for the entire company, because the reputation of the system and violations of it involve not only employees but also all stakeholders. A policy on Internet use can help companies in the following ways: (1) save employee work time; (2) prevent tying up phone lines and computer disk space that could be used for vital company business; (3) prevent exposing sensitive company data stored on computers to outside attack; and (4) prevent creations of conditions that enable employee harassment of each other and, ultimately, of the company.

Guidelines offered to employers regarding employee privacy include:

- Inform employees not to assume privacy in the workplace.
- Require employees to acknowledge the company's privacy policy in writing.
- Use private information only for legitimate purposes.
- Limit access to private information about employees to only those with a need to know.
- Secure employee medical records separately from other personnel files.
- Obtain signed permission releases and waivers before using an employee's name or photograph in any commercial advertisement, promotional material, or training film.[101]

Dating in the Workplace

As employees spend more time in the workplace, it is not uncommon for attraction and dating to occur. An annual survey of workplace romance noted that, in 2010, 60% of workers claimed to be involved in workplace romance. This is an issue that affects all employees, not just those engaging in the relationships. For example, the survey also revealed that "53.2% of those surveyed say they've known a married co-worker who had an office affair, and 40.4% say they're acquainted with a married or committed co-worker who's had a romantic liaison while on a company business trip."[102] More recently, a 2013 poll taken by work–life and benefits consultants Workplace Options reported that 84% of 18-to-29 year olds said they'd date a coworker, versus 36% of Gen X-ers (ages 30–45) and only 29% of Boomers (ages 45–65). Three-quarters of Millennials (71%) "see a workplace romance as having positive effects such as improved performance and morale. Also, 40% of millennials would engage in a relationship with a boss, versus just 12% of older employees."[103] Issues leading to liability and ethical dilemmas can arise whenever problems in the dating relationships occur, especially when one party is more powerful and demand favors from the other. Gossip, accusations, and even sexual harassment complaints can and do occur. The guidelines offered in Figure 7.4 can help protect both employers and employees.

Drug Testing and Privacy Rights

Privacy is also an issue in drug testing. Advocates for employee drug testing argue that company health costs and costs associated with sick and lost (nonproductive) days are affected when employees contract serious diseases, such

Figure 7.4

Quick Tips for Office Romance

- Find out if the company has a policy on dating; if not, check in with Human Resources or the legal/professional department
- Be professional and maintain your dignity
- Stay away from those in higher and lower positions; power differences add complexity to an already possibly gray area
- Date someone outside your work/office area if possible
- Discuss and confront personal issues after working hours and off-site
- Plan for the worst
- If relationship-related issues get too complicated, think about leaving

Source: Adapted from Doyle, Alison. (n.d.). How to handle an office romance: Tips for handling office relationships. *About.com.* http://jobsearch.about.com/od/careerdevelopment/a/office-romance.htm, accessed March 4, 2014.

as AIDS, or suffer from drug and alcohol addiction. Also, in industries (such as the airline industry or nuclear plant operations) where drug abuse can cost the lives of innocent people, screening drug abusers is viewed as in the public interest. Those who oppose forced employee drug testing argue that the practice violates employees' rights to due process and privacy.

The following guidelines can be used by companies for policy development in drug-testing programs:[104]

1. Tests should be administered only for jobs that have a clear and present potential to cause harm to others.
2. Procedural testing limitations should include previous notice to those being tested.
3. Employees tested should be notified of the results.
4. Employees tested should be informed that they are entitled to appeal the results.
5. The employer should demonstrate how the information will be kept confidential (or destroyed).

Four steps managers can take to develop corporate policy guidelines to prepare for privacy regulation in general are:[105]

1. *Prepare a "privacy impact statement."* An analysis of potential privacy implications should be part of all proposals for new and expanded systems.
2. *Construct a comprehensive privacy plan.* The privacy impact statement provides the input for planning; the plan specifies all that has to be achieved.
3. *Train employees who handle personal information.* Make employees aware of protecting privacy and of the particular policies and procedures that should be followed.
4. *Make privacy part of social responsibility programs.* Keep organizational members informed about company plans regarding privacy issues, with or without regulatory pressures.[106]

Genetic Discrimination

Should employers perform DNA testing on employees when several areas of discrimination could surface? Two examples are: (1) employment based on a person's predisposition to a disease could negatively and unfairly affect hiring, firing, and benefits; and (2) insurance companies that could obtain an employee's genetic information would also be able to deny a person certain benefits.

The following lawsuit is the first initiated by the Equal Employment Opportunity Commission (EEOC) to effectively enforce the Genetic Information Nondiscrimination Act (GINA) of 2008. This case and another (against Burlington Northern Santa Fe Railway Company in Fort Worth, Texas, also for carpal tunnel syndrome, in April 2001) emphasize the integral relationship between conduct prohibited under GINA and conduct prohibited under the Americans with Disabilities Act of 1990 as amended (42 U.S.C. §12101 et seq., Pub. L. 101-336). GINA Title II prohibits both the acquisition and the use of genetic information in employment contexts.

More recently, the case of Rhonda Jones empowered the enforcement of EEOC policy toward genetic discrimination. Jones was temporary memo clerk for Fabricut, Inc. Her temporary employment was running out when she applied for a permanent position. The company at first offered her the position before violating the GINA Title II law when, as part of its pre-employment medical examination, it allegedly requested Rhonda Jones' family history with regard to several specific conditions. "GINA defines 'genetic information' broadly to include family medical history."[107] Based on the pre-employment medical examination, Fabricut allegedly "required Jones to obtain additional testing to rule out carpal tunnel syndrome (CTS)." Even though later testing did rule out CTS, information she gave the company, Fabricut allegedly withdrew their job offer "on the basis of the pre-employment medical examination and its view that she had CTS." As part of the consent decree settling the case, Fabricut agreed to pay $50,000 in damages. The company also agreed to undertake corrective actions that include posting a non-discrimination notice to employees. GINA requires that employers post a non-discrimination notice, and "Equal Employment Opportunity is the Law" posters are readily available on the EEOC Web site. Fabricut also agreed to have its employees responsible for hiring decisions undergo non-discrimination training and further agreed to distribute non-discrimination policies to its employees.[108]

The Right to Know and Workplace Health and Safety

Every employee is entitled to a safe, healthy workplace environment, because one in 10 employees in private industry suffers from an industrial accident or disease while working. Information about unsafe, hazardous workplace conditions and some form of protection from these hazards are needed.[109] Employees have a right to know the nature and extent of hazardous risks to which they are exposed, and to be informed and trained about and protected from those risks. Right-to-know laws have been passed in 20 states since the mid-1980s.[110]

OSHA is the federal agency responsible for researching, identifying, and determining workplace health hazards; setting safety and health standards; and enforcing the standards. These remain major tasks. Critics of OSHA claim they are too overwhelming for one agency to monitor and execute effectively. The missions and budgets of government regulatory agencies—including OSHA—are also a function of the politics of the governing administration and Congress.

Smoking in the Workplace

Legislation has, or is projected to, ban smoking in public places including workplaces in several countries including the United States.[111] Among stakeholders who have argued and lobbied against smoking in the workplace are the Environmental Protection Agency (EPA), OSHA, and Action on Smoking and Health (ASH)—the powerful national antismoking group. Prosmoking advocates include the tobacco industry and its lobbying group, the Tobacco Institute, and the Bakery, Confectionery, and Tobacco Workers union. OSHA has not been able to place an absolute ban on smoking in all workplaces to date, even though tobacco has been shown to be one of the leading causes of death. The issue reflects societal habits and attitudes and the politics and economics of the industry.[112]

Consider these facts: It is estimated that 22% of adult men and 18% of adult women in America were regular smokers in 2010. Approximately 80% of workers are protected to some extent by a workplace policy, and nearly half of all indoor workers are employed in smoke-free workplaces. Twenty states and the District of Columbia have laws that restrict smoking in private-sector workplaces.[113] The American Nonsmokers' Rights Foundation stated that 81.3% of the U.S. population, as of April 2013, currently resides under a ban on smoking in "workplaces, and/or restaurants, and/or bars, by either a state, commonwealth, or local law." Almost 75% of 1,794 facility managers in a survey claim they ban or segregate smoking in their workplaces.[114]

One of OSHA's strategies has been to link smoking in the workplace to indoor air-quality problems and pollution and to legislate against it. The Clean Air Act is one such move to further restrict indoor smoking in public facilities. Employers need to keep track of laws and regulations that affect employee rights regarding smoking in the workplace.[115] Still, a bigger issue in the battle between state and federal governments and tobacco companies, at the time of writing, is over electronic cigarettes that deliver nicotine in the form of water vapor and come in different flavors. The big questions are: Who should be able to use the product? How should the product be taxed? And what, exactly, is it in the first place?[116]

The Right to Organize and Form Unions

Workers have a right to organize, just as owners and managers do. Individuals, as workers and citizens, have the right of free association to seek common ends. This also means employees have a right to form unions. Although unions have a right to exist, they have no special rights beyond those due organizations with legal status.[117]

Plant Closings and Employee Rights

Companies have the right to relocate and transfer operations to any place they choose. If firms can find cheaper labor, raw materials, and transportation costs; lower taxes; no unions; and other business advantages for making a profit elsewhere, they often close plants and move. Companies also close plants because of loss of competitiveness, financial losses, and other legitimate economic reasons. The ethical questions posed to corporate managers regarding plant closings are: What rights do the employees who are affected by the closing have? What responsibilities does the company have toward the affected communities, and even toward the national economy?

Since August 1988, companies with more than 100 employees must by law give 60 days' notice to workers before closing. Employees also have moral rights—to be treated fairly, equally, and with justice—when companies decide to relocate or close. Employees have the right to be compensated for the costs of retraining, transferring, and relocating; they have rights to severance pay and to outplacement and support programs that assist them in finding alternative employment; and they have the right to have their pension, health, and retirement plans honored.[118]

Employees also should be given the right to find a new owner for the plant and to explore the possibility of employee ownership of the plant before it is closed.[119] These rights extend beyond workers and include the welfare of the communities where the plant operates. Plant closings affect jobs, careers, families, and the local tax base, and can even negatively affect the regional and national economies, when sizable operations are shut down or moved abroad.

Whatever the motivations for corporate closings or transfer of facilities, the rights of employees and local community groups stand, even though these rights are often negotiated against the utilitarian interests of corporations in specific economic contexts. As mentioned earlier, with globalization and increased pressures on corporate profits, plant closings have become almost commonplace. Responsible employers keep employees informed of planned facility closings.[120]

The Family and Medical Leave Act

The Family and Medical Leave Act (FMLA) was enacted into law in 1993, eight years after it was introduced in Congress by Christopher Dodd, William Clay, and Patricia Schroeder. The final rules were established in 1995. The FMLA entitles eligible employees to a maximum of 12 weeks of unpaid leave per year for the birth or adoption of a child; to care for a spouse or immediate family member with a serious health condition; or when an employee is unable to work because of personal illness. The 12 weeks need not be used consecutively because intermittent leave or reduced work schedules are allowed under the act. To be considered eligible, an employee must have been employed for a continuous 12-month period and for at least 1,250 hours during the year preceding the leave.

Companies that employ at least 50 people within a 75-mile radius are mandated to offer such leave. The employer is required to maintain any preexisting

health coverage during the leave. Once the leave is concluded, the employee must be reinstated to the same position or an equivalent job. An equivalent position must have the same pay, benefits, working conditions, authority, and responsibilities.

Employers have the right to request a 30-day advance notice for foreseeable absences and may require employees to present evidence to support medically necessary leave. Employers may request employees to obtain a second medical opinion at the employer's expense. Employers may deny reinstatement of employment to "key employees." Such employees must be among the 10% highest paid company employees, and their absence must have a serious economic impact on their organization. It is the duty of employers to inform employees of their status as "key employees" when they request a leave.

Major problems with the FMLA, from employees' experience, have been serious illnesses (e.g., *Price v. City of Fort Wayne*); from employers' perspective, rising health and company costs; and from government's viewpoint, administrative requirements (e.g., *Viereck v. City of Gloucester City*). Employers often unintentionally violate the sometimes confusing and contradictory FMLA.[121] The courts have also tended to rule in favor of employees who have less serious and even minor illnesses. Finally, based on a seven-year study of more than 7,500 adults, it was found that the burden of not having a national or state-by-state family paid leave policy falls heaviest on the middle class and the working poor. Although 40% of Americans in the top quartile of income lacked a sick-leave policy at work, 54% of Americans in the second quartile, 63% in the third quartile, and 76% of workers in the bottom quartile lacked sick leave.[122] The Department of Labor's recent survey titled *Family and Medical Leave Act in 2012: Final Report* shows that FMLA "continues to make a positive impact on the lives of workers without imposing an undue burden upon employers and employers and employees alike find it relatively easy to comply with the law." More information is available on the "Wage and Hour Division" page of the U.S. Department of Labor web site (http://www.dol.gov/whd/fmla/).

7.4 Discrimination, Equal Employment Opportunity, and Affirmative Action

It is difficult to imagine that throughout most of the nineteenth century, women in America could not vote, serve on juries, issue lawsuits in their own name, or initiate legal contracts if they lost their property to their husbands. In an 1873 Supreme Court decision, *Bradwell v. Illinois,* a woman had "no legal existence, separate from her husband, who was regarded as her head and representative in the social state."[123]

It is also difficult to imagine the legal status of black people in the United States in 1857. In the Dred Scott case, one of the opinions of the Supreme

Court considered blacks as "beings of an inferior order . . . and so far inferior that they had no rights that the white man was bound to respect."[124]

More recently, discrimination has surfaced in a number of categories. Racial profiling remains an issue. Black individuals are more likely to be stopped and arrested by police than whites. Income disparities between whites and minorities continue to rise. Median wage differences and annual pay among black, white, and Hispanic men, women, and families were discussed earlier in this chapter. It is against this background that the doctrines, laws, and policies of discrimination, equal opportunity, and affirmative action must be considered.

Discrimination

Discriminatory practices in employer–employee relationships include unequal or disparate treatment of individuals and groups.[125] Unequal or preferential treatment is based on irrelevant criteria, such as gender, race, color, religion, national origin, or disability. Systematic and systemic discrimination is based on historical and institutionally ingrained unequal and disparate treatment against minorities, the disadvantaged, and women.

Examples of contemporary and systemic discrimination in employer–employee relationships are found in practices such as recruitment, screening, promotion, termination, conditions of employment, and discharge.[126] These practices are attributed to closed employment systems and practices resulting from seniority systems, "old boy networks," and arbitrary job classifications. Recruiting procedures that are biased toward certain groups and that do not openly advertise to minority groups are discriminatory. Screening practices that exclude certain groups and that use biased tests or qualifications are discriminatory. Promotion procedures that have "glass ceilings" (i.e., invisible discriminatory barriers to advancement) for women and minority groups are discriminatory.[127] Seniority tracks that favor white males or other groups over minorities or women are discriminatory. Terminating employees on the basis of sex, age, race, or national origin is discriminatory.

Equal Employment Opportunity and the Civil Rights Act

Title VII of the Civil Rights Act of 1964 makes discrimination on the basis of gender, race, color, religion, or national origin in any term, condition, or privilege of employment illegal. The law prohibits discrimination in hiring, classifying, referring, assigning, promoting, training, retraining, conducting apprenticeships, firing, and dispensing wages and fringe benefits. The Civil Rights Act also created the Equal Employment Opportunity Commission (EEOC) as the administrative and implementation agency to investigate complaints that individuals submit. The EEOC negotiates and works with the Department of Justice regarding complaints; however, the EEOC cannot enforce the law except through grievances.

The Civil Rights Act of 1991 extended, for the first time, punitive damages to victims of employment discrimination. This law states that job bias on the basis of gender, disability, religion, or national origin will be punished as severely as job discrimination based on race. It also makes it easier for job-bias plaintiffs to win lawsuits. This legislation shifts the legal burden of proof to the employer, who must defend any intentional or unintentional employment bias, especially if the practice in question has a "disparate impact" on minorities or women. Under this law, the employer must demonstrate that the alleged discriminatory act is "job-related for the position in question and consistent with business necessity."[128] "Job-related" and "business necessity" are undefined and are determined by the courts. The act specifies that employers with more than 500 employees could be liable for up to $300,000 in compensatory and punitive damages. Smaller companies are liable for less, depending on the number of workers they employ.

The Equal Employment Opportunity Act of 1972 amended the 1964 act to empower the EEOC to enforce the law by filing grievances from individuals, job applicants, and employees in the courts. All private employers with 15 or more employees fall under the jurisdiction of the revised act, with the exception of bona fide tax-exempt private clubs. All private and public educational institutions and employment agencies are covered by the law. Labor unions (local, national, and international) with 15 or more members are included. Joint labor-management committees that administer apprenticeship, training, and retraining programs are also under this law's jurisdiction.

There were 71,914 charges filed through Title VII in 2011, which resulted in recovery of $247.8 million in monetary benefits to workers who had been discriminated against.[129]

Age and Discrimination in the Workplace

The Age Discrimination in Employment Act (ADEA) of 1967, revised in 1978, prohibits employers from discriminating against individuals based on their age (between ages 40 and 70) in hiring, promotions, terminations, and other employment practices. In 1987, ADEA again was amended when Congress banned any fixed retirement age. The EEOC also issued a final rule in 2001 that aimed at prohibiting contracts requiring terminated employees to give back severance benefits if they challenged their terminations under the ADEA. "The new regulation takes effect at a time when several large corporations have announced significant layoffs. In recent years, companies have increasingly tried to tie severance deals during mass terminations to waivers of ADEA rights, as many employees who lose their jobs in such actions are over 40 and covered by the statute."[130]

Age discrimination also applies to younger individuals. Hanigan Consulting Group of New York surveyed 170 recent graduates, some scheduled to receive master's and doctoral degrees. The firm found that some applicants were asked questions that clearly violated antidiscrimination laws, such as:

Do you intend to get married and have children? What will your boyfriend think of you working long hours? How old are you? Are you married? The basic guideline, according to a Boston attorney with Seyfarth Shaw, is "if the question is not business-related and there is no legitimate business reason for asking it, then do not ask it."[131]

Comparable Worth and Equal Pay

The Equal Pay Act of 1963, amended in 1972, prohibits discriminatory payment of wages and overtime pay based on gender. The law, in large part, is based on the doctrine of "comparable worth." This doctrine and the Equal Pay Act hold that women should be paid wages comparable to men who hold jobs that require equal skill, effort, and responsibility and that have the same working conditions. This law addresses this inequity and also applies to executive, professional, sales, and administrative positions. Although women have made substantial professional progress over the past 30 years, those gains now seem to have lost momentum and even stalled. "Key indicators such as pay, board seats, and corporate-officer posts all reflect a leveling off or drop in recent years. Although the gap between men's and women's pay narrowed significantly through the 1980s, gains since then have been partly erased by a drop every few years.

Affirmative Action

Affirmative action programs are a proactive attempt to recruit applicants from minority groups to create opportunities for those who, otherwise, because of past and present discriminatory employment practices, would be excluded from the job market. Affirmative action programs attempt to make employment practices blind to color, gender, national origin, disability, and age. Although the doctrine of equal opportunity states that everyone should have an equal chance at obtaining a job and a promotion, affirmative action goes further. For example, Richard DeGeorge stated, "Affirmative action implies a set of specific result-oriented procedures designed to achieve equal employment opportunity at a pace beyond that which would occur normally."[132]

Affirmative action programs were designed to set goals, quotas, and time frames for companies to hire and promote women and minorities in proportion to their numbers in the labor force and in the same or similar occupational categories within the company.

Courts have both supported and eroded affirmative action approaches in the Civil Rights Act. Because of the changing social, political, and demographic landscape in the U.S., different membership on the Supreme Court, and evidence of reverse discrimination (see below), changes in affirmative action law are occurring. Affirmative action remains a controversial topic and policy. Individuals' rights are violated when affirmative action programs seek to protect particular groups. Also, in a market economy where individual achievement based on merit is encouraged and rewarded, it seems unfair that

arbitrary quotas should supersede those who do excel. On the other side of the controversy are advocates of affirmative action who claim that the playing field still is not level in U.S. corporate, educational, and other institutions whose officers select, hire, reward, and promote based on race, gender, national origin, ability, and other biases.

Four arguments that have been offered to explain and summarize affirmative action as it applies to hiring, promotions, and terminations are:

1. Affirmative action does not justify hiring unqualified minority group members over qualified white males. All individuals must be qualified for the positions in question.
2. Qualified women and minority members can be given preference morally, on the basis of gender or race, over equally qualified white males to achieve affirmative action goals.
3. Qualified women and minority members can be given preference morally over better-qualified white males, also, to achieve affirmative action goals.
4. Companies must make adequate progress toward achieving affirmative action goals, even though preferential hiring is not mandatory.[133]

Ethics and Affirmative Action

The ethical principles behind affirmative action are often debated. Affirmative action as a doctrine is derived from several ethical principles that serve as bases for laws.

First, the *principle of justice* can be used to argue for affirmative action, by claiming that because white males have historically dominated and continue to unfairly dominate the highest paying, most prestigious employment positions in society, members of groups who have been excluded from comparable employment opportunities because of past and present discriminatory practices deserve to be compensated through affirmative action programs embodied in equal opportunity laws. Opponents of affirmative action argue that it is unfair and unjust that the distribution of benefits be based only on a few categories (race, sex, ethnicity) rather than on achievement or other criteria.

Second, a *utilitarian principle* can be used to support affirmative action by claiming that such programs help the majority of people in a society. Opponents argue that affirmative action cannot be shown or proven to work, and suggest that its benefits do not exceed its costs.

Finally, using a *rights principle,* proponents of affirmative action can argue that protected groups have a right to different treatment because these groups have not had equal or fair access to benefits as other groups have. In fact, the rights of minorities, women, and other underprivileged groups have been denied and violated regarding access to education, jobs, and other institutional opportunities. Opponents using the rights principle argue that the rights of all individuals are equal under the law. The controversy continues as the economic, social, political, and demographic environments change.

Reverse Discrimination: Arguments against Affirmative Action

Arguments against affirmative action are directed toward the doctrine itself and against its implementation of quotas. The doctrine has been criticized on the grounds that nondiscrimination requires discrimination (that is, reverse discrimination). Reverse discrimination is alleged to occur when an equally qualified woman or member of a minority group is given preference over a white male for a job or when less qualified members of an ethnic minority are given hiring preference over white males through a quota system. Affirmative action, opponents argue, discriminates against gender and race; that is, white males. Some even say affirmative action discriminates against age: white, middle-aged males.

Another major argument against affirmative action says that individuals are held responsible for injustices for which they were not and are not responsible. Why should all contemporary and future white males, as a group, have to compensate for discriminatory practices others in this demographic category once committed or now commit?

Although these claims have some validity, proponents of affirmative action argue that injustices from discrimination have been institutionalized against minority groups. It happens that white males continue to benefit from the competitive disadvantages that past and present discriminatory practices have created for others. To compensate and correct for these systemic disadvantages based on race, gender, and other irrelevant (i.e., not related to employment) characteristics, social affirmative action goals and programs must be implemented. Still, the law is not a perfect means to correct past or present injustices. People of all races will continue to be hurt by discrimination and reverse discrimination practices. In the meantime, the court system will continue to use civil rights laws, affirmative action guidelines, and moral reasoning to decide on a case-by-case basis, the justice and fairness of employment practices.

In June 2002, the Supreme Court upheld the equal protection clause of the 14th Amendment, which guarantees equal treatment under the law by condoning the University of Michigan Law School's practice of using race to help integrate the institution's student body. The second Supreme Court opinion ruled that the admissions program in the university's undergraduate school violated the equal protection clause of the Constitution by giving minorities a bonus of 20 points in a 150-point system for race. "Two white students have sued the university claiming they were denied admission in favor of less-qualified minorities before the Supreme Court ruled. They want a federal judge to award damages to 30,000 white and Asian students who may have been illegally denied admission to make way for other minority students."[134]

Ethical Insight 7.3

The Pros and Cons of Affirmative Action

Affirmative action: Policies and procedures designed to make education and employment opportunities available to minority men and women of all races. Also created to address inequalities of present and past historical and institutional discrimination preventing persons of different races from access to education and employment in schools, universities, police and fire departments, and other public offices, as well as jobs in the private sector.

Affirmative Action

Opponents	Advocates
1. Perpetuates reverse discrimination.	1. Helps "level the playing field" by providing access to education and jobs that minorities and less advantaged groups would not otherwise be able to obtain.
2. Promotes the less qualified over the more qualified, instead of opening doors to the historically underrepresented.	2. Integrates otherwise closed institutions and corporations with individuals from diverse groups more reflective of the general population.
3. Perpetuates repressed groups continuing to be underprivileged for their benefit.	3. Is the "right thing to do." Three centuries of discrimination requires compensatory justice.
4. Disadvantages mainstream groups for injustices they did not cause and with which they do not agree.	

Questions

1. Which side of the arguments do you accept as most reasonable and realistic? Explain.
2. Why does the "Opponents" reasoning have validity?
3. Why does the "Advocates" reasoning have validity?
4. Does a level playing field exist in the society in which you live? Explain.

UCLA Law Professor Richard H. Sander argues that affirmative action programs are harmful for African American law school students because high attrition rates resulting from admitting students who fail to do the work will, in turn, turn away African American students from entering. Sander's opponents disagree with his methods and analysis. The debate over just and unfair affirmative action policies and procedures, especially in university admittance policies, continues to evolve.

7.5 Sexual Harassment in the Workplace

Sexual harassment was not a specific violation of federal law before 1981. It now may be difficult to imagine flagrant acts of sexual violation against women, but as recently as 20 years ago, when women worked in mines, they, like their male counterparts, were stripped and soaked in axle grease in a primitive hazing ritual, and then, unlike the male employees, the women were tied to wooden supports in spread-eagle positions.[135] The Senate hearings on sexual harassment charges against Supreme Court nominee Clarence Thomas awakened public and corporate concern about sexual harassment in society and the workplace. In addition, the overt sexual harassment of female U.S. Navy professionals also has brought attention to this issue. Although sexual harassment can be and is committed by both men and women, it is more often women who are the victims.

Sexual harassment remains among the most prominent civil rights issues in the workplace. There were 11,364 sexual harassment charges filed with the EEOC or state agencies in 2011, with $52.3 million paid in monetary benefits (not including monetary benefits obtained through litigation). TWA agreed to pay $2.6 million to settle a sexual harassment suit filed in 1998. The suit is one of the largest in New York State. The company will pay $1.5 million to nine women who worked in ground traffic control, passenger service, and maintenance. The *New York Times* reported that three women "accused three high-level managers of egregious sexual harassment that included groping and verbal abuse." Lawyers for the women said that the airline did nothing about repeated complaints taken to different levels of management before the suit was filed. Other sexual harassments have resulted in multimillion dollar settlements. A lawsuit against the large building-maintenance company ABM Security Services brought by 21 Hispanic female workers resulted in a $5.8 million settlement, in which the company admitted no wrongdoing. Charges included touching, sexual comments, requests for sex, and even rape. A 1998 suit against Mitsubishi Motors by female plant workers at the company's Normal, Illinois plant resulted in a $34 million settlement. The company now has a "zero tolerance policy in place for sexual harassment."[136] More recently, a meta-analysis on sexual harassment showed an organization's climate was a factor in sexual harassment incidences. Also victims experienced post-traumatic stress disorder, loss of work, decreased organizational commitment, poor job satisfaction, and problems with physical and mental health.[137]

What Is Sexual Harassment?

The Supreme Court ruled in 1986 that sexual harassment is illegal under Title VII of the 1964 Civil Rights Act and that when a "hostile environment" is created through sexual harassment in the workplace, thereby interfering with an employee's performance, the law is violated, regardless of whether economic harm is done or whether demands for sexual favors in exchange for raises, promotions, bonuses, and other employment-related opportunities are granted.[138]

Under Title VII, the EEOC guidelines (1980) define sexual harassment as follows:

> Unwelcome sexual advances, requests for sexual favors, and other verbal or physical conduct of a sexual nature constitute sexual harassment when (1) submission to such conduct is made either explicitly or implicitly a term or condition of an individual's employment, (2) submission to or rejection of such conduct by an individual is used as the basis for employment decisions affecting such an individual, or (3) such conduct has the purpose or effect of unreasonably interfering with an individual's work performance or creating an intimidating, hostile, or offensive working environment.

The courts have defined sexual harassment as conduct ranging from blatant grabbing and touching to more subtle hints and suggestions about sex. Forms of sexual harassment include the following: [139]

- Unwelcome sexual advances.
- Coercion.
- Favoritism.
- Indirect harassment.
- Physical conduct.
- Visual harassment. (For example, courts have ruled that sexual harassment was committed when graffiti was written on men's bathroom walls about a female employee and when pornographic pictures were displayed in the workplace.)

More women are speaking out under the protection of Title VII of the amended Civil Rights Act, which is discussed later in this chapter. Sexual harassment continues to be reported across industries, including outstanding companies such as Wal-Mart. Moreover, men's sexual harassment charges increased to 16.4% of all sexual harassment charges filed to the EEOC in 2010, compared to only 11.6% in 1997.[140] These statistics do not show whether the alleged harassers of men were also men, although they generally are. Diversity training programs are now offered in many larger reputable U.S. firms.

Who Is Liable?

The EEOC guidelines place absolute liability on employers for actions and violations of the law by their managers and supervisors, whether or not the conduct was known, authorized, or forbidden by the employer. Employers also are liable for coworkers' conduct if the employer knew, or should have known, of the actions in question, unless the employer shows, after learning of the problem, that the company took immediate and appropriate action to correct the situation. Employers may be liable for harassment of nonemployees under the same conditions as those stated for coworkers.[141]

Moreover, under EEOC guidelines, employers are responsible for establishing programs (and standards) that develop, train, and inform employees

Figure 7.5

Sample Corporate Sexual Harassment Policy

1. Sexual harassment is a violation of the corporation's EEO policy. Abuse of anyone through sexist slurs or other objectionable conduct is offensive behavior.
2. Management must ensure that a credible program exists for handling sexual harassment problems. If complaints are filed, they should receive prompt consideration without fear of negative consequences.
3. When a supervisor is made aware of an allegation of sexual harassment, the following guidelines should be considered:
   a. Obtain information about the allegation through discussion with the complainant. Ask for and document facts about what was said, what was done, when and where it occurred, and what the complainant believes was the inappropriate behavior. In addition, find out if any other individuals observed the incident, or similar incidents, to the complainant's knowledge. This is an initial step. In no case does the supervisor handle the complaint process alone.
   b. If the complaint is from an hourly employee, a request for union representation at any point must be handled as described in the labor agreement.
   c. The immediate supervisor or the department head and the personnel department must be notified immediately. When a com-plaint is raised by, or concerns, an hourly employee, the local labor relations representative is to be advised. When a complaint is raised by or concerns a salaried employee, the personnel director is to be advised.
4. The personnel department must conduct a complete investigation of the complaint for hourly and salaried employees. The investigation is to be handled in a professional and confidential manner.

Source: Based on the General Motors corporate policy on sexual harassment.

about sanctions and procedures for dealing with sexual harassment complaints (see Figure 7.5). It is in the employer's economic and moral interest to institute such programs, because courts mitigate damages against companies that have harassment prevention and training programs. Some of the leaders in establishing sexual harassment policies and programs are NYNEX, AT&T, DuPont, Corning, and Honeywell, to mention only a few.

Tangible Employment Action and Vicarious Liability

A currently prominent feature of harassment cases is the concept of "tangible employment action," which Supreme Court Justice Anthony Kennedy described as "hiring, firing, failing to promote, reassignment with significantly different responsibilities or a decision causing a significant change in benefits."[142] An employer's defense against claims of harassment has been created in cases in which a hostile environment was evident but no tangible employment action occurred. In the Supreme Court decision in the case *Burlington Industries v. Ellerth:*

> Kimberly Ellerth's harasser threatened to take steps against her if she didn't comply with his wishes. Since he never carried out the threat, Ellerth's

employment status was not negatively affected. However, her harassment was severe and pervasive, and Burlington was held liable for that instead.[143]

Severe and pervasive harassment that has no tangible employment action characterized another case, *Faragher v. City of Boca Raton*. In this case, it was determined that lifeguard Beth Faragher had been repeatedly harassed by two male supervisors for several years. She complained to other beach supervisors, but to no avail. Attorneys for the city argued that she had not complained to authorities at a high enough level. This defense laid the foundation for another key concept the Court stressed: "vicarious liability."[144]

Employers, under this concept, could be liable for harassment if it is committed by *anyone* present in the workplace and if it is brought to the attention of *any* manager or supervisor. Employers are liable for harassment by anyone who is present in the workplace (coworkers, customers, vendors), if the employers know or should have known about the harassment. Moreover, employers are liable for harassment by all supervisors, whether the employer knew about the harassment or not. This represents a significant change in sexual harassment liability.

Employer Guidelines with Extended Liability Rulings

Employers should:

- Exercise reasonable care to prevent and correct for any harassment. There should be an antiharassment policy and a complaint procedure present, made known to every employee, readily available, and used in training. The EEOC enforcement guidelines provide an excellent source of training materials.
- Quickly and effectively address all harassment complaints.[145]

Individual Guidelines

Although sexual harassment often occurs as part of a power issue (i.e., people in more powerful positions exert pressure over people in less powerful posts), a frequent observation is that men and women tend to see sexual harassment differently. This certainly does not justify legally or morally unwelcome sexual advances. It does suggest, however, that employers need to provide adequate education, training, and role-playing between the sexes so that gender differences in perceptions and feelings on what constitutes sexual harassment can be understood. Some practical guidelines that employees (men, in this instance) can use to check their motives and behavior regarding sexual harassment include the following:[146]

- If you are unsure whether you have offended a woman, ask her. If you did offend her, apologize, and don't do it again.
- Talk over your behavior with noninvolved women and with men you can trust not to make a mockery of your concerns.

- Ask yourself how you would feel if a man behaved toward your daughter the way you feel you may be behaving toward women.
- Ask yourself also if you would act this way if the shoe were on the other foot, if the woman were your boss or if she were physically stronger or more powerful than you.
- Most of all, don't interpret a woman's silence as consent. Silence is, at least, a "red light." Through silence, a woman may be trying to send you a signal of discomfort. Be very certain that your comments or behaviors are welcome, and if they are not, stop them.

Sexual Harassment and Foreign Firms in the United States

Two foreign companies operating in the United States have reacted differently to sexual harassment charges; this is a perilous area where the law and societal norms are rapidly changing. These companies' reactions have exposed them to increased liability. One of the firms, Astra, a Swedish pharmaceutical firm, fired its CEO of the U.S. subsidiary and two other top managers. The other company, Mitsubishi, has denied all charges; has maintained that EEOC is wrong; and has mounted a full-scale public relations campaign to discredit complainers. Both companies lacked one of the most basic requirements consultants recommend: a clear and strongly written policy on sexual harassment.[147]

Companies have the obligation of training and supporting their employees who work and conduct business internationally on harassment and discrimination laws. "When in Rome, do as the Romans do" does not mean do nothing, act immorally, or act from your own intuition as an employee representing your company. As Figure 7.6 illustrates, many countries have specific laws on employment discrimination and sexual harassment. Some are not the same as those in the U.S. For example, Venezuela, as of January 1, 1999, has a new employment discrimination statute that prohibits sexual harassment and punishes this crime by a prison term from 3 to 12 months. The offender must also pay the victim twice the amount of economic damage in regard to lack of access to positions, promotions, or job performance that resulted from the sexual harassment.[148]

7.6 Whistle-Blowing versus Organizational Loyalty

The decision to become a whistle-blower frequently requires breaking with the very group that we have viewed as critical to our financial success, if not our very survival. The decision entails destabilizing one's life and placing all the essential underpinnings of our financial security—and the security of those who depend on us—at total risk. It is easy to understand that such a decision is accompanied by a good deal of anxiety and stress.[149]

Among all the rights discussed in this chapter, one of the most valued by a U.S. citizen is freedom of speech. But how far does this right extend into

Figure 7.6

Survey of Harassment and Its Crimination Law

Jurisdiction	Prohibitions on Employment Discrimination	Prohibitions on Sexual Harassment	Legal Basis
Argentina	Yes	Yes, by judicial ruling	Section 16, Argentine Constitution
Australia	Yes	Yes	Race, Sex, and Disability Acts
Belgium	Yes	Yes	Article 10, Belgian Constitution; Royal Decree of September 19, 1997
Brazil	Yes	No	Article 5, Brazilian Constitution; Section 461, Brazilian Labor Code
Canada	Yes	Yes	Human rights laws of each province
Chile	Yes	Yes	Article 19, Constitution; Article 2, Labor Code
Colombia	Yes	No	Article 53, Constitution; Article 10, Labor Code
Czech Republic	Yes, by judicial decision	No	Decision No. 13/94, Constitutional Court
Egypt	Yes	No, except by extension of Civil Code	Article 40, Constitution
France	No	Yes	Article L 122-46, French Labor Code; Article 27, Law of December 31, 1992
Germany	No	Yes	Section 2, Article 31, Constitution; Disability Act; Employee Protection Act
Hong Kong	Yes	Yes	Sex Discrimination Ordinance; Disability Discrimination Ordinance
Hungary	Yes	No	Article 5, Hungarian Labor Code
Ireland	Yes	Yes	Employment Equality Act
Italy	Yes	Yes, by judicial decision	Law No. 125 of April 10, 1991

Figure 7.6 *—continued*

Japan	Yes	Yes	Equal Employment Opportunity Act
Mexico	No	Yes	Section 153, Mexican Penal Code
Netherlands	Yes	Yes	Article 3, Dutch Labor Conditions Act; Article 7, Dutch Civil Code
People's Republic of China	Yes	No	Article 12, Labor Law of the PRC (1995)
Philippines	No	Yes	Republic Act 7877 (1995)
Poland	Yes	No	Articles 32 and 33, Constitution; Labor Code
Republic of South Africa	Yes	No	Act No. 66, South African Labor Reform Act of 1995
Russia	Yes	No	Russian Labor Law of 1995
Singapore	Yes; age only	No	Retirement Act
Spain	Yes	Yes	Articles 9, 14, and 35, Spanish Constitution; Section 34.3.95 of Spanish Employment Act
Sweden	Yes	Yes	The Act on Equal Opportunities at Work
Switzerland	No	Yes	Article 3, Law on Equal Treatment of Women and Men
Taiwan	No	Yes	Article 83, ROC Social Order Maintenance Act
Thailand	Yes	Yes	Constitution; Labor
Ukraine	Yes	No	Article 42, Labor Code of the Ukraine
United Kingdom	Yes	Yes	Sex, Race, and Disability Discrimination Laws
Venezuela	No	Yes	Law on Violence Against Women and Family

Source: Adapted with permission from Maatman Jr., Gerald. (September 11, 2000). Harassment, discrimination laws go global. *National Underwriter, 104(37),* 3.

the corporation, especially if an employee observes an employer committing an illegal or immoral activity that could harm others? What are the obligations and limits of employee loyalty to the employer? Under what, if any, circumstances should employees blow the whistle on their supervisors, managers, or firms?

Whistle-blowing is "the attempt of an employee or former employee of an organization to disclose what he or she believes to be wrongdoing in or by the organization."[150] Whistle-blowing can be internal (reported to an executive in the organization); external (reported to external public interest groups, the media, or enforcement agencies); personal (harm reportedly done only to the whistle-blower); and impersonal (harm observed as done to another).[151] Whistle-blowing goes against strong U.S. cultural norms of showing loyalty toward an employer and colleagues and avoiding the "snitch" label. However, strong cultural norms regarding fairness, justice, a sense of duty, and obedience to the law and to one's conscience also exist. A moral dilemma can occur when a loyal employee observes their employer committing or assisting in an illegal or immoral act and must decide what to do.

The whistle-blower may not only lose his or her job but may also experience negative and damaging repercussions in his or her profession, marriage, and family life. Dr. Jeffrey Wigand, head of research at Brown and Williamson Tobacco Company from 1989 to 1993, testified that this company knew and controlled the nicotine levels in its products. His testimony, along with that of others, helped the government initially win a substantial lawsuit against the tobacco industry. As the film *The Insider* accurately documented, Wigand paid an enormous personal price as a witness.[152]

Not all whistle-blowers undergo such traumatic fates as the example offered here. Michael Haley, a federal bank examiner, won $755,533 in back pay, future loss of income, and compensatory damages under the federal whistle-blower statute and another amended federal statute. He had worked as a bank examiner for the Office of Thrift Supervision (OTS), starting in 1977. He inspected OTS-regulated banks, evaluating the soundness of their operations. He was terminated after he reported violations in federal banking laws and regulations regarding a forced merger.[153]

Under what conditions is whistle-blowing morally justified? DeGeorge discusses five conditions:[154]

1. When the firm, through a product or policy, will commit serious and considerable harm to the public (as consumers or bystanders), the employee should report the firm.
2. When the employee identifies a serious threat of harm, he or she should report it and state his or her moral concern.
3. When the employee's immediate supervisor does not act, the employee should exhaust the internal procedures and chain of command to the board of directors.
4. The employee must have documented evidence that is convincing to a reasonable, impartial observer that his or her view of the situation is

accurate and evidence that the firm's practice, product, or policy seriously threatens and puts in danger the public or product user.
5. The employee must have valid reasons to believe that revealing the wrongdoing to the public will result in the changes necessary to remedy the situation. The chance of succeeding must be equal to the risk and danger the employee takes to blow the whistle.

The risks to whistle-blowers can range from outright termination to more subtle pressures, such as strong and hidden criticisms, undesirable and burdensome work assignments, lost perks, and exclusion from communication loops and social invitations.[155] Although 21 states have laws protecting corporate and governmental whistle-blowers from reprisal, experience shows that the government's actual protection to whistle-blowers, even if after resigning or being fired they are reinstated with back pay and compensation for physical suffering, is weak because of the many subtle forms of retaliation, such as those just listed.

The Whistleblower Program proposed under the Dodd-Frank Wall Street Reform and Consumer Protection Act took effect on August 12, 2011. This program offers monetary awards to eligible whistle-blowers for information provided to the Securities and Exchange Commission (SEC). To be eligible, the tip provided to the SEC must be of high-quality information and must lead to a "Commission enforcement action in which over $1,000,000 in sanctions is ordered. The range for awards is between 10% and 30% of the money collected." Although this provides incentive for the disclosure of potential fraud to the SEC, it may also have negative repercussions for companies and whistle-blowers. Companies now have greater motivation to prevent whistle-blowing to the SEC, as SEC action may lead to monetary sanctions, loss of reputation, and other damage.[156]

When Whistle-Blowers Should Not Be Protected

The most obvious condition under which whistle-blowers should not be protected is when their accusations are false and their motivation is not justifiable or accurate.

The following instances are when whistle-blowers should not have freedom of speech against their employers:

- When divulging information about legal and ethical plans, practices, operations, inventions, and other matters that should remain confidential and that are necessary for the organization to perform its work efficiently.
- When an employee's personal accusations or slurs are irrelevant to questions about policies and practices that appear illegal or irresponsible.
- When an employee's accusations do not show a conviction that a wrongdoing is being committed and when such accusations disrupt or damage the organization's morale.

- When employees complain against a manager's competence to make daily work decisions that are irrelevant to the legality, morality, or responsibility of management actions.
- When employees object to their discharge, transfer, or demotion if management can show that unsatisfactory performance or violation of a code of conduct was the reason for the decision.[157]

Factors to Consider before Blowing the Whistle

Whistle-blowing is a serious action with real consequences. It often involves a decision to be made among conflicting moral, legal, economic, personal, family, and career demands and choices. No single answer may appear. A stakeholder analysis can help the potential whistle-blower identify the groups and individuals, stakes, priorities, and trade-offs when selecting among different strategies and courses of action.

The following 12 guidelines offer factors that a person should consider when deciding whether to blow the whistle on an employer:[158]

1. Make sure the situation warrants whistle-blowing. If serious trade secrets or confidential company property will be exposed, know the harm and calculated risks.
2. Examine your motives.
3. Verify and document your information. Can your information stand up in a hearing and in court?
4. Determine the type of wrongdoing and to whom it should be reported. Knowing this will assist in gathering the type of evidence to obtain.
5. State your allegations specifically and appropriately. Obtain and state the type of data that will substantiate your claim.
6. Stay with the facts. This minimizes retaliation and avoids irrelevant mudslinging, name-calling, and stereotyping.
7. Decide whether to report to internal contacts or external contacts. Select the internal channel first if that route has proven effective and less damaging to whistle-blowers. Otherwise, select the appropriate external contacts.
8. Decide whether to be open or anonymous. Should you choose to remain anonymous, document the wrongdoing and anticipate what you will do if your identity is revealed.
9. Decide whether current or alumni whistle-blowing is the best alternative. Should you blow the whistle while you are an employee or resign first? Resigning should not be an automatic option. If the wrongdoing affects others, your decision is not only a personal one, but you are also fulfilling moral obligations beyond your own welfare.
10. Follow proper guidelines in reporting the wrongdoing. Check forms, meeting deadlines, and other technicalities.
11. Consult a lawyer at every step of the way.
12. Anticipate and document retaliation. This assists your effectiveness with courts and regulatory agencies.

Managerial Steps to Prevent External Whistle-Blowing

Managers have a responsibility to listen to and respond to their employees, especially regarding the observations of and reporting of illegal and immoral acts. Chapter 6 discussed mechanisms such as "ethics offices," ombudsperson programs, and peer review programs. These are part of a corporation's responsibility to provide due process for employees to report personal grievances, to obtain effective and just resolution of them, and to report the wrongdoings of others, including the employers. Four straightforward and simple steps management can take to prevent external whistle-blowing are:[159]

1. Develop effective internal grievance procedures and processes that employees can use to report wrongdoings.
2. Reward people for using these channels.
3. Appoint senior executives and others whose primary responsibilities are to investigate and report wrongdoing.
4. Assess large fines for illegal actions. Include executives and professionals who file false or illegal reports, who knowingly market dangerous products, or who offer bribes or take kickbacks.

Preventing, reporting, and effectively and fairly correcting illegal and immoral actions, policies, and procedures are the responsibilities of employers and employees. Management cannot expect employees to be loyal to a company that promotes or allows wrongdoing to its stakeholders. Whistle-blowing should be a last resort. A more active goal is to hire, train, and promote morally and legally sensitive and responsive managers who communicate with and work for the welfare of all stakeholders.

Chapter Summary

The demographics of the workforce at the beginning of the twenty-first century continue to change. These changes include the aging of employees, the "shrinking" of the workforce, an increasing number of women and minority entrants, the demand for work–life balance from singles and dual-career families, the gap in educational levels, and a greater demand for the skills of disabled workers. The changes in the composition of the workforce signal changes in work-related values and motivations. Corporations and managers can expect moral tensions to rise regarding issues such as age discrimination, health care needs, conflicting communication, generational differences, and requests for more balanced and flexible work schedules. "One size fits all" management techniques do not work.

The social and psychological contract between corporations and employees is also changing. The original employment-at-will doctrine serves as the basis for employment between employer and employee; however, over the years, this doctrine has been complemented by the doctrine of implied employee rights. Most firms, large and small, use a mix of the two doctrines. Two underlying concepts of employee rights are balance and governmental rights.

The nature of legal and moral relationships between employers and employees is also changing. Employers rely on federal and state laws to guide their employee policies and procedures. However, many employers implement benefits and policies aimed at motivating and supporting employees' well-being. Work–life resources and insurance coverage for employees' same-sex partners are such examples.

Recent court decisions have supported racial affirmative action practices at the university admittance level. Although EEOC policies and affirmative action practices remain a part of federal law, some states are showing less acceptance of these laws and procedures. Current and future issues related to sexual harassment and reverse discrimination will continue to shape legal and moral guidelines for corporations. Conflicts regarding due process, privacy, safety, drug testing, sexual harassment, technology monitoring, and other workplace topics will continue to be resolved through court cases and legislation; their resolution will influence corporate policies in the future.

Sexual harassment laws and guidelines for employers and employees and the moral dilemma of organizational loyalty versus personal ethics will always be important issues. The justification for whistle-blowing and guidelines for potential whistle-blowers must be considered by employees before blowing the whistle and by corporations to prevent external whistle-blowing.

Questions

1. Identify two major trends in the changing demographics of the workforce. Include a trend that you as a student or employee could be or are now affected by.
2. Identify moral tensions and/or conflicts that could lead to illegal and/or unethical behavior associated with the changes you gave in question 1.
3. What are three major factors an employer should consider to avoid arbitrarily terminating an employee? What steps would you take if you were terminated by an employer who arbitrarily fired you?
4. What problems do you see occurring when employees date in a company? What additions or changes would you make to the tips and suggestions offered on dating in the chapter?
5. What does the term legal and moral entitlement mean to you as an employee or future employee? Give an example. Do you agree that employees have legal and moral entitlements in the workplace? Explain.
6. Do you believe dating should be permitted among employees in the workplace without formal policies setting boundaries and rules? Why or why not?
7. Do you believe managers and company officers should date lower level employees with less power and status? Why could this situation present ethical dilemmas?
8. What are some changes that have occurred as a result of the Civil Rights Act of 1991?

9. Do you believe there is now an "equal playing field" regarding access to educational institutions, jobs, and other employment opportunities for all individuals and groups in the United States? Explain. Do you believe women should still be a protected group under Title VII of the Civil Rights Act? Explain. Do you believe minorities of different races in the U.S. other than Caucasian should still be protected? If so, which group(s)? If not, explain why not.
10. What are some arguments for and against "reverse discrimination?" Is the "playing field" in U.S. corporations more level now?
11. Describe criteria used to determine whether verbal or physical actions constitute sexual harassment. What are some specific types of sexual harassment? Have you been sexually harassed in a work setting? Can you describe what happened and the outcome?
12. What should employees expect from their employers and their companies now in terms of rights and obligations? Explain. Is loyalty to an employer a "dead" or "dying" concept now? Why or why not?
13. Do you believe whistle-blowing is justifiable in corporations? Would, or could, you blow the whistle? Under what circumstances would you be compelled to blow the whistle as an employee in an organization? Offer an example.
14. Should corporate managers prevent whistle-blowing? Why or why not? Explain.
15. How can employers prevent whistle-blowing?

Exercises

1. Argue the pros and cons of eliminating standards such as test scores, grade point averages, and other objective criteria for admitting minorities and members of protected groups to universities and colleges. Do you believe such objective criteria should be eliminated by university and college admissions committees? Explain.
2. Select an employee right in the workplace from the chapter. Give an example, based on your own outside reading or experience, of a situation involving this right. Was it violated? How? What was the outcome? What should the outcome have been? Why?
3. Identify an example from your own experience, or that of someone you know, of discrimination or sexual harassment. Did this experience influence your view of affirmative action or employee protection programs? If so, how?
4. Write a paragraph describing a situation from your experience in which you felt justified that you had cause to blow the whistle. Did you? Why or why not? Under what circumstances do you feel whistle-blowing is justified?
5. Think of three people you know from the different generations discussed in the chapter. Of these people, who is and is not satisfied with their work and jobs? Explain why they are or are not satisfied. Refer back to the generational

differences and values in the chapter. To what extent did "generational differences" contribute in your analysis of the individuals' work satisfaction? To what extent did "ethical reasons" affect their work satisfaction? Explain.

6. Create a "for" and "against" set of arguments regarding the "employment-at-will" doctrine in the present economic and demographic environment. After you make a complete set of arguments, which position do you support? Did your views change after this exercise? Why or why not?

Real-Time Ethical Dilemma

What's Going on Here?

Bill Smith and Lana Kane seemed to have had some "bad chemistry" the day they met. Bill, 23, a recent graduate and now working on his MBA, has been with the Marketing Group for a year. He is eager to excel, thrives on instant (especially positive) feedback, and is accustomed to participative, entrepreneurial work relationships. Upper-level management has been impressed with his work and has given him "free reign" on most assignments, since the Marketing Group had been without a director for the past year. Lana, 51, has been with the company for nine years and has just been assigned to head up the Marketing Group. Lana is accustomed to a more structured, orderly approach and also takes her seniority seriously. Bill was preparing a presentation on a new promising product launch for the company's CEO and officers when he found an e-mail from Lana asking to review and approve his presentation before he submits it to Ralph, the CEO.

Lana's e-mail was critical of several of Bill's ideas, and she asked to meet with him. At their one-on-one meeting the following afternoon in Lana's office, they immediately started clashing. Lana politely but straightforwardly read her responses to Bill's e-mail, and Bill couldn't remain silent. He challenged her on every point, refusing to accept her logic. Lana grew tense and finally lashed out at Bill saying, "Can't you be more open to different perspectives? My role is to offer criticism to improve our efforts, not only to always give praise." Bill was frustrated and hurt that Lana couldn't see the same talent in him that upper management saw. "Why is she so stubborn and controlling?" he thought as he folded up the paper with her comments about his presentation. Nervously pondering the situation before leaving her office, he thought, "Maybe I should talk to Ralph about her. If I have to work with this style, I should pack my bags today." At the same time, when Lana looked at Bill's expressions, she thought, "I'm not sure this guy 'gets it.' He's bright but too spoiled, and not tough-skinned enough to take helpful criticism. I wonder if I should talk to HR [human resources] about him?"

Questions

1. What are the problems in this situation?
2. What potential "ethical" dilemma or issue could arise from this situation?
3. What perspective(s) in this chapter could help diagnose this evolving issue?
4. What should be done to prevent an issue from erupting into a conflict and between whom?

Cases

Case 19

Preemployment Screening and Facebook: Ethical Considerations

Introduction

In 2006, researchers at the University of Dayton surveyed over 5,000 employers nationwide and found a surprising trend brought on by the rapid growth of online social media: 40% of employers had considered the Facebook profile of a potential employee as part of their hiring decision (Wiley). As Facebook's popularity has increased, so too did the number of employers using Facebook to vet job applicants. "Recruiting has always been an art, but it's becoming a science," says Dan Shapero. More and more employers are using otherwise personal information in recruiting decisions. In 2009, a study by Microsoft found that over 70% of recruiters and human resource (HR) departments had rejected candidates or rescinded offers after checking Facebook and related social networking web sites.

As if job seekers didn't already have enough to contend with—criminal background checks, drug tests, credit reports, and verification of employment history, education, income, etc. are among the most common forms of pre-hire scrutiny used by employers today—now it appears social media, Facebook in particular, has become a deciding factor in who gets hired—and fired—in today's workforce. The volume of résumés typically received for open positions makes it more efficient for recruiters to conduct online searches than to conduct reference checks. With nearly 50% of resumes containing factual errors, employers contend that they are acting in the best interest of the firm by erring on the side of caution when it comes to hiring.

According to Beth E. H. Lory, lead employer relations coordinator for the career services office at the University of Minnesota, traditional college-aged students (18 to 22 years of age) are affected the most by this emerging trend since they post more videos, pictures, thoughts, experiences, and observations on Facebook than any other group. Chris Wiley, associate director of career services at the University of Dayton and lead researcher of the 2006 employer survey cited earlier, explains further: "Since Facebook was originally created by college students for college students, they view it as 'their place' and strictly a social network."

However, in the eyes of potential employers, students' Facebook profiles often raise questions about their judgment, eliminating them as job candidates. "The term they've used over and over is red flags," says Trudy G. Steinfeld, executive director for the center of career development at NYU. "Is there something about their lifestyle that we [as employers] might find questionable or that we might find goes against the core values of our corporation?" When viewed by corporate recruiters, such pages can make college graduates looking to join the

workplace appear immature and unprofessional. This raises the all-important question of whether a Facebook profile accurately portrays an individual. Regardless of the answer, the fact is that the majority of employers today are basing their hiring decisions, at least in part, on information found on Facebook.

Certainly, there is nothing inherently wrong with "rejecting an applicant with personal characteristics that will negatively affect job performance. That is part of any employer's mandate," say Texas-based lawyers Peter G. Smith and Whitt L. Wyatt. However, when employers obtain such information through social media "they are unable to ensure that all the information they uncover will be job-relevant"—and most would agree that one's online social life is *not* job-relevant. Law often lags behind on issues surrounding technology—preemployment screening using Facebook is currently unregulated—but it doesn't seem like this will be the case for very long. In addition to questioning Facebook's legitimacy (i.e., its relevance and reliability) in the recruiting process, many are beginning to wonder if using Facebook to evaluate potential employees is a violation of personal and informational privacy, not to mention if there are unintended consequences stemming from this uniquely Digital Age practice. Although it is important for employers to know who they are hiring, it is unethical to use Facebook to achieve this goal on the basis of privacy and fairness.

Ethical Considerations

"[Facebook] is becoming very much a common tool," said Warren Ashton, group marketing manager at Microsoft. "For the first time ever, you suddenly have very public information about any candidate." Many companies who have used information retrieved on Facebook in their recruiting process champion this belief, believing all user-generated content on the Internet is "public," so long as it is legally accessible. In other words, all nonproprietary, noncopyrighted information available on the Internet is fair game for employers to use as they wish. However, this self-serving interpretation of "fair use" is incomplete and morally irresponsible. Heidi Perman, assistant director of the campus career center at the University of Minnesota says, "Just because [employers] have access to the information does not make it right for [them] to get it." Information on Facebook is of a personal nature and it should be approached (or not approached) the same way, since all people have an appreciable, albeit unspoken, right to privacy.

According to Facebook's "Statement of Rights and Responsibilities": "You own all of the content and information you post on Facebook, and you can control how it is shared through your privacy settings." When a Facebook user posts personal information on their profile and then limits that information to a specific network, such as his/her alma mater or online friends, there is a reasonable argument that this information should be considered private. One issue with this defense, however, is that the default setting for various Facebook applications (e.g., profile picture, political affiliation, relationship status) enables anyone with a Facebook account to access this information. More often than not, recruiters have no trouble viewing candidates' Facebook profiles because said privacy settings have not been utilized. Alternatively, if an employer searches a candidate's

profile and finds it is blocked, a new issue can arise since employers may wonder why and assume he/she must be hiding something.

HR professionals and recruiters will sometimes ask candidates to "friend" them on Facebook before continuing to second round interviews. This tactic is not only deceptive, but it also subjects candidates to a host of personal biases. What ought to be an objective assessment of relevant job skills becomes a subjective judgment of "character." The lengths to which employers are willing to violate personal and informational privacy to view information that was more than likely never intended for them raises an even greater ethical issue surrounding the use of Facebook in the recruiting process: how employers are interpreting and using this information for their hiring decisions.

For most, Facebook is a vehicle for casually interacting with others in an informal setting. In this light, Facebook users post and share information intended for their friends, rather than considering the impact their content may have with potential employers. Not surprisingly, 64% of students ($N = 2{,}000$ undergraduates from colleges and universities nationwide) said employers should not consider Facebook profiles during the hiring process. Results from a similar survey conducted in 2010 by the National Association of Colleges and Employers (NACE) indicate that "less than one-third of responding seniors think employers should be looking at their profiles." Students' opinions aside, the same NACE survey found that "more than a third of responding employers said they found information that caused them not to hire a person applying for the job, including provocative or inappropriate photographs [and] content related to drinking or using drugs."

To put it in a context that may resonate with employers from older generations who never had to contend with Facebook to progress in their careers, Peter Engler and Peter Tanoury, MBA students from the University of Colorado's Leed School of Business, say "recruiters' actions are similar to job applicants following a group of executives on their Sunday morning round of golf and listening to all of their conversations . . . [and] then forming an idea about the firm as a whole and deciding if they wanted to work there." In this analogy, it is unlikely these executives would censor their conversations because they are in an open forum, despite the fact there is no physical privacy. Candidates' Facebook profiles warrant the same privacy that the executives would demand—and deserve—during their hypothetical round of golf. This analogy not only resonates back to the issue of personal and informational privacy discussed earlier, but it also alludes to the issue of fairness in the context of using irrelevant and potentially inaccurate information to make hiring decisions.

Although the majority of employers are using Facebook to discern the "right men (and women) for the job," some companies, including Enterprise Rent-a-Car, Ernst & Young, and Osram Sylvania, say they do not use social media to screen job applicants. "I'd rather not see that part of them," said Maureen Crawford Hentz, manager of talent acquisition at Osram Sylvania. "I don't think it's related to their bona fide occupational qualifications." Hentz makes a valid point—even if one's online persona was a reflection of who one is as a person and the types of

decisions one makes (in one's personal life), the information on Facebook has no bearing on how one will perform in the workplace and therefore should not be factored into an employer's hiring decision.

Technology has a long-standing habit of blurring the lines between people's personal and professional lives, but it is the responsibility of both employers and employees to preserve these boundaries. Of course, it is impossible to completely separate the two, but that doesn't give employers the right to determine one's professional merits from an information source that is strictly personal. After all, there's a reason employers don't conduct reference checks of friends and family—and the same reason applies to using Facebook to evaluate potential employees. A case can be made that employees in sales, public relations, and customer service, or any higher-level managerial position function, are representatives of their company. Therefore, companies have a legitimate concern for how their employees behave off-the-clock.

However, this justification is missing one crucial element: context. For example, in the case of the recent college graduate, the missing context is professional responsibility; that is, holding one accountable for actions that took place prior to his/her employment. Potential employees cannot be held to the same behavioral standards as current employees, especially in this example, given the differences in maturity pre- and postcollege graduation. More fundamentally, what place does an employer have dictating what an employee—or rather, *a person*—does on his/her own time, so long as it's legal and not specifically prohibited in the company's code of conduct? Professional responsibility notwithstanding, it is unfair, and therefore unethical, for employers to use Facebook as an ideological litmus test and consider the perceived social habits of job applicants during the recruiting process.

The ethical issue of fairness not only revolves around the relevance of the information on candidates' Facebook profiles, but also around the reliability of this information. "It's easy to paint an entire picture without context and make inaccurate assumptions based on limited information," says Heidi Perman, "[but] as someone who hires, I don't look at Facebook." Without the appropriate context, even factual information can be misinterpreted. For example, let's say a user lists "partying" as one of his interests. To the user, "partying" may simply consist of having a drink or two with a few friends on Friday night, but to a potential employer, "partying" may be interpreted as irresponsible binge drinking. Facebook screening is often conducted in the earlier parts of the recruiting process, therefore the unsuspecting candidate in this example would likely never be given a chance to correct the inaccurate, negative impression. He would be eliminated prior to being given an interview.

Of course, there's also the possibility for employers to misinterpret false information. For example, "in one instance a female user was a member of the group 'Future Trophy Wives of America.' Although a college student would look at this as a joke or think nothing of it at all, an employer may take this as fact and assume the female would only work for a few years before marrying and quitting." Engler and Tanoury's example is consistent with the University of Dayton study, which

found that 23% of students said they intentionally misrepresented themselves to be funny. Both of these examples resonate back to the question of whether a Facebook profile accurately portrays an individual–and prove that it does not. The *ethics of justice* (i.e., principle of fairness) purports that everyone be treated equally, and in the case of employment, that each candidate be given a fair chance to be considered for the position he/she is seeking. Consequently, using Facebook in the recruiting process and basing hiring decisions on information taken out of context, that may or may not be true, is an unfair and unethical practice.

Legal Considerations

Although no laws specifically prohibit this practice, employers run the risk of violating other laws. The Fair Credit Reporting Act (FCRA), for example, "requires employers to notify job applicants and obtain their consent before conducting a background check." Though the current FCRA guidelines do not apply to the preemployment screening of social media, experts agree that it is only a matter of time. The Employment Practices Data Protection Code states that an employer "should not place reliance on information collected from possible unreliable sources . . . [and] employers should only use pre-employment vetting as a means of obtaining specific information, not as a means of general intelligence gathering." The Employment Practices Data Protection Code echoes both the issues of privacy and fairness. The following elements of this code were designed to protect the rights of individual citizens and consumers with regard to their privacy from either intentional and/or unintentional data collection, sharing, and use by and between organizations:

- Some personal information (e.g., sex and race) would normally be obtained through a conventional interview. But other information such as country of origin, religious preference, pregnancy, age, disability or sexual orientation might not.
- Employers . . . increase their exposure to discrimination claims when they gather too much [protected] information about a candidate. The Equal Employment Opportunity Commission (EEOC) provides a list of certain classes of information that employers are generally prohibited from asking an applicant. The list is as follows: age, disability, genetic/family information, national origin, pregnancy, race/color, religion, sex/sexual orientation, and political views. These classes of information are considered "protected information" under federal civil rights laws, including Title VII of the Civil Rights Act, the Americans with Disabilities Act (ADA) and the Age Discrimination in Employment Act (ADEA). Under federal law, employers must demonstrate that the information gained by inquiring into one or more of the above-referenced classes is relevant to determining an applicant's fitness to perform the job. Otherwise, such inquiries are presumed discriminatory by the employer.

  "When an employer visits a person's social web site, the employer is instantly given access to everything that person has chosen to share with the world. Much of the information is not protected by law but also is not relevant to the job. In addition to the legal duty of the employer not to discriminate based

upon a person's protected characteristics, there is also an ethical duty for the employer not to discriminate based upon any characteristics that do not affect the job. Often the mere appearance of discrimination is enough for an employer to face a discrimination lawsuit."

Proposed federal legislation titled the Social Networking Online Protection Act (SNOPA) could make it illegal for employers to require prospective employees to provide passwords and other confidential information necessary to access their social-networking accounts as a prerequisite to employment. The proposed bill by Eliot Engel (NY-D) and Jan Schakowsky (IL-D) introduces pioneer legislation that would make such invasive practices unlawful in today's technological era. If passed, any employer violating the provisions of SNOPA could face a $10,000 civil penalty.

Practical Considerations

Employers' utilitarian approach to preemployment screening isn't effective, nor does it reduce harm/serve the "greater good": "When examining this issue, it is also important to understand the ethical framework from which employers justify their actions. Whether knowing it or not, when an employer uses Facebook as a means for employment screening they are practicing the utilitarian approach of ethics. Under this approach, *the ethical corporate action is the one that produces the greatest good and does the least harm for all who are affected*—customers, employees, shareholders, the community, and the environment. In the context of employment screening, this means that employers will dig as deep as possible into the personal lives of their applicants, using any means necessary (such as Facebook), in order to hire the best employees who will in turn increase shareholder value."

Final Comment

The argument is not that it is wrong for employers to know about their applicants before hiring an employee, but that Facebook is not the means to acquire this information.

Questions for Discussion

1. What are the main ethical issues regarding social media users and employers?
2. Do you think it is ethical to use social media, such as Facebook, in employment considerations? Explain.
3. Do you think some information a person communicates on Facebook is private and confidential? If not, then isn't all information on Facebook potentially public? If so, then what is the problem with employers using and making decisions with that information?
4. Would it be ethical if Facebook profited from selling your and others' personal information to employers? Why or why not?

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Case 20

Women on Wall Street: Fighting for Equality in a Male-Dominated Industry

Allison Schieffelin and Morgan Stanley

On June 12, 2004, Morgan Stanley agreed to pay $54 million to settle dozens of claims from women who alleged that the securities firm denied them pay increases and promotions due to their gender. The case, filed by the Equal Employment Opportunity Commission (EEOC) on September 10, 2001, resulted from repeated complaints by Allison Schieffelin, a 43-year-old former convertible-bond sales clerk who worked in the firm's institutional-stock division for 14 years. Schieffelin earned more than $1 million a year, making her one of the highest-paid and highest-ranking women on Wall Street to publicly challenge the industry's pay and promotion practices. Schieffelin claims that she was trapped under a glass ceiling and continuously denied promotion to managing director despite being the top performer in her department. The EEOC claims that in addition to being repeatedly denied promotions and pay raises, women employees in Schieffelin's division "endured coarse behavior and lewd comments from their male colleagues and supervisors." Moreover, firm-organized sales outings with clients to golf resorts and strip clubs excluded women.

Of the $54 million settlement, $12 million was paid directly to Schieffelin. About $40 million will be used to settle complaints from an estimated 100 current and former female employees of the institutional-stock division. The remaining $2 million was used to enhance anti-discrimination training at the firm. In addition to the monetary settlement, Morgan Stanley must also fund a program to have an appointed outsider monitor hiring, pay, and promotion practices for a three-year period. Although the settlement seems large, it is merely "pocket change" to a firm like Morgan Stanley; the $54 million represents approximately 2% of the $2.45 billion in profits the firm earned in the first half of fiscal year 2004.

Background on the *Schieffelin et al. v. Morgan Stanley* Case

Allison Schieffelin first complained of Morgan Stanley's working environment in a 1995 written review of her boss stating, "He makes the convertible department and the firm by extension an uncomfortable place for women." During that same year, she also submitted an internal complaint about "unwelcome advances" from one of her male managing directors. At the time, she thought that management would be pleased with the tactful manner in which she handled the issues; however, today she feels management placed her on a "watch list" instead.

In December 1998, after three years of withstanding the men's locker-room type atmosphere, in which the male employees openly "swapped off-color jokes and tales of sexual exploits and treated their female colleagues as inferior," Schieffelin took her harassment and discrimination complaints beyond the firm's executives to the EEOC. She hoped that the firm would see that she had been a dedicated employee throughout her entire career and that the issues with the

firm's pay and promotion practices needed to be amended. Instead, she claims the firm "embarked on a campaign to get me to quit." She was fired in October 2001 for what the firm claims to be misconduct after a heated confrontation with her supervisor; however, both Schieffelin and the EEOC viewed her firing as illegal retaliation for her discrimination complaints. One year after Schieffelin complained, Morgan Stanley's New York convertibles department, the department in which Schieffelin worked, promoted Gay Ebers-Franckowiak to managing director—the first female managing director in that department; many people believe that this was no coincidence.

Morgan Stanley denied all discrimination charges and claimed that their female employees were and are treated equally. The EEOC planned to reveal evidence at the trial proving otherwise. The anticipated evidence indicated that some male employees of the firm ordered breast-shaped birthday cakes and hired strippers to entertain at office parties. The evidence supposedly provided statistics regarding the disparities between female and male promotion and pay within the firm. The trial was scheduled to begin July 12, 2004; however, a settlement was wrapped up mere minutes before opening arguments began. As part of the settlement, payroll statistics that showed whether or not there was a pattern of discrimination were sealed.

An Isolated Occurrence or an Industry-Wide Problem?

The allegations made against Morgan Stanley are not new to the securities industry. Several previous cases, in addition to statistics produced by the Securities Industry Association (SIA), indicate that sex discrimination is a persistent problem on Wall Street.

In April 2004, Merrill Lynch agreed to pay $2.2 million to Hydie Sumner as part of a class-action lawsuit brought by more than 900 women claiming the financial giant had a long history of gender discrimination. Sumner wanted her old job back; she also said that she wanted to be a Merrill Lynch manager in order to make changes at the firm. "I thought, one day, I'll be a manager and I'll have a choice, and I won't manage like him [Stephen McAnally, former manager of the Merrill Lynch San Antonio office]," said Sumner. As of early 2005, Merrill Lynch paid Sumner $1.9 million but was fighting the other $300,000, indicating that this payment would "not be considered until the issues relating to Ms. Sumner's reinstatement at the firm are resolved."

In a more recent lawsuit, Stephanie Villalba, former head of Merrill Lynch's private client business in Europe, sued for $13 million on gender-bias charges. She claimed that her male boss had difficulty accepting her in a senior position and, as a result, she was "bullied, belittled, and undermined." In early 2005, an employment tribunal in the United Kingdom ruled in favor of "Villalba's claim of victimization on certain issues, that included bullying e-mails in connection with a contract, but found no evidence of a 'laddish culture' at the bank." Villalba intends to appeal the ruling.

In February 2004, Susanne Pesterfield, a former broker for Smith Barney, settled her case with the investment firm on the eve of an arbitration hearing.

She alleged that during her seven years at the firm she endured a "pattern of sexual harassment and a male-dominated culture that included trips to strip clubs." She described a working environment that was "hostile to women and in which women weren't given the same opportunities to succeed as men were given." She claimed that her male colleagues were better paid and received better leads for potential clients.

Pesterfield's accusations were not new to Smith Barney. A class-action lawsuit brought by female employees in 1996 led to a 1998 settlement in which the firm's parent company, Citigroup, Inc., paid out close to $100 million. The infamous case has been referred to as the "Boom-Boom Room," in reference to the basement "party room" in the Garden City branch of what was then Shearson Lehman Brothers, wherein discrimination and sexual harassment occurred. Among other things, the conversations that took place among the male employees went beyond their accomplishments on the trading floor to include their latest accomplishments in the bedroom. Shearson's manager took a "boys will be boys" approach that encouraged obscene comments and lewd behavior.

In her book, *Tales from the Boom-Boom Room,* Susan Antilla provides a detailed account of the workplace culture at Shearson. According to Antilla, "it was a time when men in branch offices of brokerage firms were encountering significant numbers of female colleagues for the first time. For some of them, it was unsettling." In the late 1990s, many well-educated women entered the financial services industry in hopes of finding great opportunities. Instead, they found an industry that continued to be dominated by white males and an environment that belittled and repressed women.

The acts of alleged sex discrimination abound; nearly 3,000 women filed claims in 1996 and 1997 against Smith Barney and Merrill Lynch. Although most of the women settled, some did not, including Nancy Thomas, Sonia Ingram, Laura Zubulake, Deborah Paulhus, and Neill Sites. Perhaps most notable is the case of Nancy Thomas, a broker at Merrill Lynch for 18 years. Among the numerous allegations of sex discrimination made by Thomas, one is particularly salacious. Thomas alleges that in 1991 "someone left her a package in the mailroom with a dildo, lubricating cream, and an obscene poem." An arbitration hearing was held in New York on September 13, 2004; arbitrators scheduled an additional 18 hearing sessions through July 2005. Merrill Lynch maintained that none of the testimony given as of late November 2004 "support[ed] even one of Thomas's allegations."

Wall Street's Glass Ceiling—The Numbers Tell the Story

The *2003 Report on Diversity Strategy, Development & Demographics* produced by the SIA presents data suggesting there has been little improvement in the advancement of women in the securities industry in recent years, and that biased pay and promotion practices are not just outdated. Even though Wall Street firms seem to be making attempts to improve the workplace environment for women, statistics prove that a strong glass ceiling still exists. There was a gradual decrease in the percentage of women in the industry between the years

1999 and 2003 (43% and 37%, respectively), and management positions in 2001 and 2003 continued to be dominated by white males. In 2003, white males held 85% of (branch) office manager positions, 76% of the managing director positions, and 79% of the executive management positions. This compares to 85%, 81%, and 75% for the three position categories in 2001. The same is true for line positions such as brokers (80% in 2001 versus 78% in 2003), investment bankers (77% versus 71%), and traders (71% versus 74%). On the other hand, "white women and men and women of color continue to comprise the majority (89%) of the staff and junior level positions."

These numbers become even more disturbing when one considers that women are not new to the profession. In 1974, women held 33.8% of all securities industry jobs with 6.5% being management positions. Muriel F. Siebert, chair of Muriel Siebert & Co. and the first woman with her own seat on the New York Stock Exchange, has worked on Wall Street since the 1950s. She claims that highly educated and successful women are consistently "dropping out" of the industry and changing careers because they feel they have no chance of reaching top management positions.

Catalyst, a nonprofit research organization working to advance women in business, conducted a study of female professionals in the securities industry. Published in 2001 as *Women in Financial Services: The Word on the Street,* the results indicated the top three barriers to women's advancement were lack of mentoring opportunities, commitment to personal and family responsibilities, and exclusion from informal networks of communication. The survey also highlighted the differences in the viewpoints of male and female professionals with respect to the advancement of women. While 65% of women believed they had to work harder than men to get the same rewards, only 13% of men believed this to be true; 51% of women felt they were paid less than men for doing the same work, while only 8% of men agreed with this statement. In addition, 50% of men believed that women's opportunities to advance to senior leadership in their firms had increased greatly over the preceding five years, but only 18% of women agreed. Many of the women who file complaints, as well as their lawyers, maintain that the perceptual divide between genders is a serious issue. They argue that the men in charge at Wall Street firms do not recognize the existence of a problem, and therefore they fail to look at the statistics and to see the "big picture."

Mandatory Arbitration and Coercion Prevent Statistics from Appearing in Court

In 1986, the Supreme Court ruled that sexual harassment is illegal under Title VII of the 1964 Civil Rights Act. However, recent statistics and settlements in gender discrimination suits suggest that the glass ceiling, at least within the securities and investment banking businesses, still exists. What makes Wall Street such a laggard when it comes to the treatment and advancement of women? One factor could be that before 1999 any employee of a Wall Street firm was required to resolve all disputes in a "closed-door negotiation process" rather than in a public hearing. As the rest of corporate America was hit with discrimination

lawsuits in the 1980s and 1990s, the problems occurring on Wall Street remained, for the most part, behind closed doors. After the Boom-Boom Room case and the Merrill Lynch suit in the late 1990s, the Securities and Exchange Commission removed the mandatory arbitration requirement for Wall Street employees who had civil-rights claims. As a result, "the National Association of Securities Dealers and the New York Stock Exchange changed their arbitration rules in a way that permitted employees to sue under federal discrimination statutes in federal court."

Why Should the Securities Industry Make Changes?

Sex discrimination lawsuits have been costly, in terms of money and negative publicity, for securities firms. Avoiding such costs in the future is a strong motivation for change, but not the only one. Another powerful reason is the increasingly influential role of women in business. In 1998, women owned close to 8 million U.S. businesses, which was one-third of the total, and "more than 40% of households with assets of $600,000 or more [were] headed by women." In 2004, 10.6 million firms were at least 50% female-owned; 48% of all privately held firms were at least 50% female-owned.

Moreover, as more working women approach retirement age and younger women rise in the ranks, securities firms desire to increase their female clientele. As a result, there is an increasing demand for female brokers to serve the needs of this "new" client base. Women investors tend to prefer doing business with a friendly, trustworthy adviser rather than just a person with financial expertise, and thus they aim to establish a personal relationship with their brokers/advisers. To serve an increasingly diverse client base, investment firms must recognize that they will need a diverse group of employees who recognize and react appropriately to the needs of their clients.

In 2013, one of the United States' largest privately held life insurers, New York Life, recently announced its plans to hire up to 3,700 new agents with at least half being women or individuals representing (in the company's own words) "cultural markets," under which it includes individuals "serving the African American, Chinese, Hispanic, Korean, South Asian, and Vietnamese markets." This will be in addition to the 62% of new hires last year in those categories. Like publicly traded insurer Allstate, whose staff is made up predominantly by women (58.9%), New York Life understands that having a staff that represents a gender- and racially diverse subset is going to give it a better chance to grow its business.

Who Wins, Who Loses?

Richard Berman, the judge in *Schieffelin et al. v. Morgan Stanley,* described the $54 million settlement as a "watershed event in protecting the rights of women on Wall Street." Many others, including Elizabeth Grossman, an EEOC lawyer on the case, hope that the settlement will act as a revelation for not only Morgan Stanley but other Wall Street firms as well. The settlement may cause other firms within the securities and investment banking industry to reevaluate their pay and promotion practices. Additional complaints may also surface because of the settlement.

Although some people view the settlement in a positive light, others see a negative side. As part of the settlement, claimants agreed not to disclose any of the statistics and facts that would have been presented in the case. Although the women who will share the $54 million settlement scored a big win, some people believe that Morgan Stanley and other securities firms "scored an even bigger win" by preventing embarrassing statistics from being revealed in the courtroom and to the public.

The securities and investment banking firms seem to have a "what the public doesn't know, won't hurt them" attitude. Unless the compensation and promotion statistics of those firms are exposed to the public, Wall Street businesses will continue operating within its current culture. In "Money Talks, Women Don't," an article about the Morgan Stanley settlement, Susan Antilla stated, "Ingrained cultural misconduct changes only when customers, colleagues, and the public get wind of the nasty facts and companies are embarrassed. Those who can afford to keep their problems quiet may never have to change."

Today on Wall Street

Some aspects of work on Wall Street have improved for women, but changing the culture of an entire industry cannot happen overnight, especially if firms are reluctant to admit that a problem exists. Antilla suggests that there has been reluctance to address the discrimination and harassment issues even after they were revealed in the Boom-Boom Room and Merrill Lynch lawsuits of the late 1990s: "When it came to acknowledging that there was still a problem to work on—violators to stop and biases to correct—Wall Street had become a little like the dysfunctional family hiding the crazy uncle in the attic. Everyone knew sexual harassment was there and indeed had put much energy into urgently and quietly negotiating the crises that resulted from it. But hardly anyone spoke openly about the problem—called the doctor, if you will—and started the real work of making things better."

Today, firms are more likely to have diversity programs and sexual harassment training. Many companies have altered their recruiting processes and several have established partnerships with support organizations that promote equal opportunities in professions for women and minorities. Some companies are working at changing the "tone at the top" by promoting women to top positions and challenging old attitudes within the companies. For example, in late 2002 Smith Barney hired its first woman chief executive, Sallie Krawcheck. Since then, the company has fired some of its most successful brokers for mistreating female coworkers, thereby sending a message that such behavior will not be tolerated—even in the most valued employees. Despite these efforts, the industry statistics and continual lawsuits suggest that women in the financial services industry are not playing on a level playing field quite yet.

Indeed, as one Wall Street observer, Dan Ackman, a columnist for *Forbes* magazine, noted, "beyond the numbers, nearly every woman on Wall Street will tell you there are, to this day, subtle and not-so-subtle double standards and a still pervasive atmosphere of harassment." And as the business writer John Churchill

reports, "Many complainants claim the firms have just become subtler in their discrimination, rigging teams, for instance, so that when men retire or change firms, the most lucrative accounts they leave behind get assigned to other members of the old-boy network, not to the most senior broker in the office." Consequently, the most important question with respect to sexual discrimination in the securities and investment banking industry may be: What must happen in order for a true and pervasive cultural change to take place on Wall Street?

Questions for Discussion

1. Is business ethics relevant to the topic and examples in this case or is this just business as usual? Explain.
2. What are the ethical implications of the one-time arbitration requirement that prevented Wall Street employees from seeking redress through the court system?
3. Why is the securities and investment banking business male-oriented and dominated?
4. Why does sex discrimination seem to persist on Wall Street in spite of the negative publicity of lawsuits and monetary costs of settlements?
5. What can or should be done to transform the persistent culture of sex discrimination on Wall Street?
6. Would you like working on Wall Street as a woman? Explain.
7. As a man or woman, what lessons would you take from this case if you accepted a professional job in a Wall Street firm?

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8

BUSINESS ETHICS AND STAKEHOLDER MANAGEMENT IN THE GLOBAL ENVIRONMENT

8.1 The Connected Global Economy and Globalization

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OPENING CASE

The new global economy is no longer comprised of separate economies per country or region; instead, it has become a complex grid of interconnected networks of resources. Advances in technology have made it possible for "money, goods, data, and people to cross borders in huge volumes and at unprecedented speed. Since 1990, trade flows have grown 1.5 times faster than global GDP. Cross-border capital flows have expanded at three times the rate of GDP growth."[1] Consider that now "only one in ten US dollars in circulation today is a physical note – the kind you can hold in your hand or put in your wallet. The other nine are virtual. Estimates by Cisco Systems suggest that in 2009, global

data flows expanded by nearly 50 percent. In China alone, more than 150 million new people connected to the Internet in 2009, giving that country a digital population almost as large as the world's biggest social-networking site, Facebook." Emerging markets–like Brazil, China, and India–are strongly impacted by this new global grid. "The explosion of mobile networks is giving billions of people their first real entry point into the global economy, helping them become more informed consumers, connecting them with jobs, and providing much better access to credit and finance."[2]

Consider also the impact globalization has on the business community. A growing global information grid directs companies toward new innovations and connections to the Internet. John Deere tractors, for example, are equipped with GPS guidance systems "to apply fertilizers to cropland precisely. TomTom has created systems of 'smart' traffic lights that improve traffic flows. Nortura, Norway's largest food supplier, uses radio-frequency identification (RFID) technology to trace chickens from the farm to the store shelf."[3] Borders have been blurred with the increase in connectivity, and companies can operate in multiple countries. Decisions made and actions taken can now affect a much broader base of stakeholders. New cultural challenges and growth opportunities are facing globalized businesses.

If you are a new or an experienced hire in a global company, or in a firm facing these challenges, you may have "your work cut out for you." You may also want to "globalize" your own thinking and skills–if you haven't already–and gain awareness of the wider ethical impacts of your work, your company, and your stakeholders–in international settings. Your ethics may be challenged as well in the old but newly developing world.

8.1 The Connected Global Economy and Globalization

The global environment consists of a dynamic set of relationships among financial markets, cultures, politics, laws, technologies, government policies, and numerous stakeholders and stakeholder interests. The new "flat world" consists of hypercompetition from different regional players across the globe. This global environment also involves individual citizens, families, and communities that are—and many that are not—served by multinational enterprises (MNEs). This chapter presents different dimensions of globalization that affect new and experienced managers and professionals, and people in every nation. Ethical Insight 8.1 defines and describes globalization in this broader context.

Ethical Insight 8.1

What Do We Mean by Globalization?

"The Earth's current population of some 6.5 billion is expected to rise to 8.0 billion by 2030, an average increase of 60 million annually. More than 97 percent of this growth will take place in developing countries. The output of the global economy will rise from $35 trillion in 2005 to $72 trillion in 2030. Though the incomes of developing countries will still be less than one-quarter of those in rich countries in 2030, they will continue to converge with those of wealthy countries. Developing countries' share in global output will increase from about one-fifth of the global economy to nearly one-third." As this new "global middle class" emerges, many are left behind. Inequalities are faced, in particular, by unskilled workers. "While developing countries are closing the income gap with rich countries, as many as two-thirds—more than 80 percent of the developing world outside China—may experience a worsening of within-country inequality."

What do we mean by globalization? Globalization is about an increasingly interconnected and interdependent world; it is about international trade, investment, and finance that have been growing far faster than national incomes. It is about technologies that have already transformed our abilities to communicate in ways that would have been unimaginable a few years ago. It is about our global environment, communicable diseases, crime, violence, and terrorism. It is about new opportunities for workers in all countries to develop their potential and to support their families through jobs created by greater economic integration.

But globalization is also about international financial crises, about workers in developed countries who fear losing their jobs to lower-cost countries with limited labor rights. And it is about workers in developing countries who worry about decisions affecting their lives that are made in far-away head offices of international corporations. Globalization is therefore about risks as well as opportunities. We must deal with these risks at the national level by managing adjustment processes and by strengthening social, structural, and financial systems. And at the global level, we must establish a stronger international financial architecture and work to fight deadly diseases, to turn back environmental degradation, and to use communications to give voice to the voiceless.

We cannot turn back globalization. Our challenge is to make globalization an instrument of opportunity and inclusion—not of fear and insecurity. Globalization must work for all. There are more challenges ahead, and bigger ones. As we go forward, the voices of the poor must be our guide.

Time is short. We must be the first generation to think both as nationals of our countries and as global citizens in an ever-shrinking and more connected planet. Unless we hit hard at poverty, we will not have a stable and peaceful world, shaped by the decisions we make, and the courage and leadership we show today.

Sources: Wolfensohn, J. D. (April 2, 2001). The challenges of globalization: The role of the World Bank. *WorldBank.org.* http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:20025027~pagePK:34370~piPK:42770~theSitePK:4607,00.html, accessed Jan-

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We begin by identifying the forces underlying the globalization process in general, and then present ethical issues which companies in the global environment face. Business and ethical competencies that managers and professionals need to compete when doing business internationally are presented. We then discuss the societal "dark side" of ethical issues and globalization, followed by a presentation of MNEs as stakeholders and their host-country relationships. We conclude by identifying negotiation methods for making ethical decisions, taking cross-cultural contexts into consideration.

Globalization and the Forces of Change

Because globalization involves the integration of technology, markets, politics, cultures, labor, production, and commerce, it encompasses the processes and results of this integration. The economic benefits of globalization are both large and measurable. Globalization "expands trade flows and allows consumers to enjoy a range of goods and services vastly larger than that produced by their domestic economy. International financial flows enhance the efficiency with which capital and know-how are allocated."[4] The global economy has been estimated at $33 trillion. Although globalization has facilitated economic growth over several decades, this process is also vulnerable to forces in the environment, as discussed in this chapter. The most recent threats to economic stability and growth are the national bankruptcies and debt crises across the globe (like Greece, Italy, and the United States), subprime lending crisis, out-of-control investment practices, dysfunctional governmental regulation, rising oil and energy prices, environmental catastrophes (like the 2011 earthquake in Japan), and global terrorism, all of which continue to generate costs to businesses and the public. Nevertheless, technological emerging markets and innovation continue to support the globalization process. Some of the forces fueling this include the following:

- The end of communism and the rise of the so-called EMEs (emerging market economies) in Asia, Latin America, Europe, Russia, Africa, and the Middle East. Both of these developments have added to the growth of the global economy, as discussed in the opening case. Although this growth is cyclical, countries in these regions show continuing strength in their economic development.[5] As noted above, the rise of EMEs means greater business competition. An Ernst & Young report noted the increasing global power of emerging markets as one of the six global trends shaping the business world. "Rapid population growth, sustained economic development

and a growing middle class are making many companies look at emerging markets in a whole new way. Many companies that had previously posed no competitive threat to MNEs now do so. Working to serve customers of limited means, the emerging market leaders often produce innovative designs that reduce manufacturing costs and sometimes disrupt entire industries. A case in point: India's Tata Motors' US$2,900 Nano, priced at less than half the cost of any other car of the market worldwide."[6]

- Global corporations invested more in emerging markets than the core economies of the United States, Europe, and Japan for the first time, according to the United Nations Conference on Trade and Development (UNCTAD) in their 2013 *World Investment Report*. Developing economies also absorbed more foreign direct investment (FDI) than did the developed ones; and four developing economies ranked among the five largest recipients in the world. China ranked first in this category. Developing countries generated nearly one-third of global FDI outflows, which continued the trend of cash-rich corporations in foreign countries investing in the advanced economies. The European Union (EU) accounted for nearly two-thirds of the global FDI decline.[7]
- The emergence of China as a global manufacturer and U.S. trading partner (now the second largest world economy), and India as a source of world-class offshore technology services. The U.S. goods deficit with China increased from $273.1 billion in 2010 to $295.5 billion in 2011.[8] China and India's growth rates may experience a slowdown because of the subprime and other financial crises, but the prominence of these two countries in the global economy continues to grow.
- Information technologies and the Internet also accelerate communication and productivity within and across companies globally. Today it is fairly easy for any company to globalize using the Internet. Japanese companies seem to have mastered the strategy of using globalized supply chains, controlling 70% of the global market share of 30 different technology sectors with $1 billion or more in revenues. Technological innovations have helped spur this globalization. Superconductors, for example, will be economically ready for many daily applications and will advance to commercial use after 2015. Tools like the Internet as a sales platform and virtual sourcing are transforming the way global businesses operate. New technologies should continue to improve the efficiency of many industries while lowering costs.
- Free trade and trading agreements continue among nations with open borders, among which are the EU free trade agreements (see Figure 8.1 for a list of these countries); the North American Free Trade Agreement (NAFTA), which encourages large and small businesses to operate in Canada and Mexico; the Association of Southeast Asian Nations (ASEAN), which helps emerging companies to compete with European and U.S. firms; and the World Trade Organization (WTO), which accepted China starting in 2002 and which provides a framework that "creates stability and predictability

so that investors can, with more security, plan their activity."[9] Global trade has tripled over the past 25 years, and trading relationships are changing. Asia, for example, has surpassed both the United States and Europe to become the largest trading partner of the Middle East. New relationships, like that of China and Africa, are emerging. The trading partnership between China and Africa has been growing annually by 30%.[10]

- In the longer term, China could well seek to import much more food from Africa, which, by World Bank estimates, has 60% of the world's uncultivated land. "Given Africa's potential, China is likely to turn towards it."[11] The China–Africa relationship will get stronger. The editors of *China Returns to Africa* sum it up: So long as Africa's development requires huge foreign investments, so long will China continue to be relevant. "Irrespective of the concerns being voiced in some circles in Africa, Chinese involvement is widely considered to be a positive-sum game."[12]
- The National Intelligence Council recently commissioned a report on global trends extending to the year 2030. Over the next two decades, the report notes, the relative power of major international actors will shift markedly. Around 2030, China is predicted to be the largest world economy. In 2030, India will become the third largest economy and the world's most populous country. Brazil's economy will rank fourth. India, Brazil, and China will, as superpowers, be making international political decisions alongside the United States, even as the relative weight of Russia and Japan diminishes. "The European economy will remain in the top tier, but it is not clear whether Europe will be able to act with common purpose to leverage this source of strength."[13]
- The World Bank and the International Monetary Fund (IMF) offer a conduit for needed capital flows to countries participating in building the global economy—as China, India and emerging economies continue to gain wealth and influence. The euro and other Asian currencies will slowly but steadily compete to replace the U.S. dollar as the global basis of exchange rates. China currently holds over $3.18 trillion in U.S. foreign reserves.[14]
- "Global terrorism" and counter-responses since September 11, 2001, continue to present regions, countries, and businesses with sizable risks and costs. A 2011 Congressional Research Service report calculated that, following September 11, the United States has spent a cumulative total of $806 billion on the war with Iraq, $444 billion on the war with Afghanistan, $29 billion for enhanced homeland security, and $6 billion of unallocated funds. It is projected that war costs could require an additional $496 billion over the next 10 years. For the fiscal year 2010, the U.S. Administration noted a cost of $1 million per troop per year in Afghanistan alone, and monthly war obligations in 2010 cost an average of $11.1 billion.[15] The continuing costs of preventing and managing terrorist risks in the United States and other countries is substantial to the global economy and to affected industries, such as the U.S. airlines.

- Multinational enterprises (MNEs) continue to grow, open new markets, and create jobs across the globe. Of the world's top 100 economies in 2009, only 53 were countries; 34 were cities and the remaining 13 were corporations. The top countries are still the United States and China, with India now at number four; and the top corporations are Royal Dutch Shell and ExxonMobil.[16] Examples of such transnational giants include Wal-Mart, BP, Toyota Motor, General Electric, Texaco, British Petroleum Amoco, Ford, Procter & Gamble, Coca-Cola, and Heinz. An estimated 40,000 to 100,000 multinational companies continue to do business across national boundaries and contribute to the global economy. It is likely these numbers will increase. Where there are new markets, companies will move and be created. At the same time, MNEs will spend more on risk management, which in turn will encourage outsourcing, rather than investing in offshore facilities that are vulnerable to political instability.
- Global poverty and income disparity are also major factors. "Half the world—over three billion people—live on less than $2.50 a day. At least 80% of humanity lives on less than $10 a day. More than 80 percent of the world's population lives in countries where income differentials are widening. The poorest 40 percent of the world's population accounts for 5 percent of global income. The richest 20 percent accounts for three-quarters of world income."[17] However, the global poverty rate was cut in half between 1990 and 2010.[18]

Growth also decreases poverty: growth has frequently been much more effective at reducing poverty in countries with low-income inequality than in countries with high-income inequality. Promoting equality, particularly among different religious, ethnic or racial groups, also helps reduce social conflict.[19]

But as countries continue to grow, possibilities for positive change can occur. If poverty falls at its current rate, the number of people living at

Figure 8.1

European Union Country Members

Austria	Italy
Belgium	Latvia
Bulgaria	Lithuania
Croatia	Luxembourg
Cyprus	Malta
Czech Republic	Netherlands
Denmark	Poland
Estonia	Portugal
Finland	Romania
France	Slovakia
Germany	Slovenia
Greece	Spain
Hungary	Sweden
Ireland	United Kingdom

$1.20–1.25 a day will also fall: to 56 million in 2020 and 28 million in 2030. However, unless growth trends dramatically upward, "it is not possible to maintain the trend rate of poverty reduction with so many fewer individuals ready to cross the line." The geography of poverty will be transformed. China passed the point years ago where it had more citizens above the poverty line than below it. By 2020, there will be hardly any Chinese left consuming less than $1.25 a day; everyone will have escaped poverty. But there is still a long way to go. According to UNICEF, "22,000 children die each day due to poverty. . . . Nearly a billion people entered the 21st century unable to read a book or sign their names." There are 2.2 billion children in the world; 1 billion live in poverty.[20] These conditions create and add to the instability of governments, the rule of law, and political regimes; and to the influence of global terrorism.

- Consumers are demanding social responsibility from corporations. "Over 88% of consumers think companies should try to achieve their business goals while improving society and the environment and 83% of consumers think companies should support charities and nonprofits with financial donations." Furthermore, "the average American consumer will drive nearly 11 minutes out of their way to buy a cause-marketing product and nearly two-thirds of employees would seriously consider leaving their job if their employer used child labor in sweatshop factories." Certain programs and initiatives are now expected of companies by consumers, for example, recycling programs and the prevention of child labor.[21]
- A shift to service economies and knowledge workers using technologies has also propelled innovation and productivity worldwide. The rise of the service economy has been clearly driven by high-skill industries. The importance of low-skill service industries in value-added has actually declined. Knowledge workers will work in flatter, more networked, geographically dispersed organizations. Leadership will be shared and individual professionals will be required to work in virtual as well as land-based teams as electronic communications accelerate. "When agents can only home produce for themselves, two additional forces contribute to the rise of the service economy: (1) as the wage increases, high-skilled individuals demand more market services as the opportunity cost of home producing services increases; (2) as the quantity of high-skilled individuals increases, the demand for market services increase as high-skilled individuals consume more market services relative to low-skilled individuals."[22]

8.2 Managing and Working in a "Flat World": Professional Competencies and Ethical Issues

As the forces driving globalization indicate, this process is complex with results that differ in benefits and burdens depending on who the stakeholders are. We identify and discuss major effects of globalization on these different stakeholders in this chapter. We continue with the professional entering the

global workforce. As the opening case indicated, globalization brings hypercompetition and challenges to new and continuing leaders and professionals in corporations. This section begins with three questions: (1) Is there an ideal profile of competencies for global managers and professionals who will work in different countries? (2) Is there a global set of values and ethics that benefits transnational companies, their managers, and professionals? (3) What are ethical issues these professionals might expect to find? The following quote by David Tai, director of Human Resource (HR) Learning at IBM India/South Asia, who prepares employees for global leadership, is relevant here: "Today's global economy is a knowledge economy, which requires fresh thinking and innovative approaches to workforce management. In fact, IBM's latest human capital management study reveals that 75 percent of global business leaders are worried about the ability to build globally aware leaders; 88 percent of those respondents are from Asia."[23]

There is a demand for "a new type of cosmopolitan, multinational, multifaceted executive who is operational across national borders."[24] Brian Hum, an HR specialist in globalizing workforces, noted that there are two preconditions that must be met for international business managers to adapt successfully: "They must want to operate effectively in another culture and they must be excited by the challenges ahead. Attempting to learn a foreign language to a reasonable standard is another favorable indicator. International business managers need to be sensitive to foreign cultures with no sign of prejudice. Their ability to cope with ambiguity, particularly when dealing with different business cultures and ethical dilemmas is an essential competence. . . . Previous overseas experience . . . is not necessarily an indicator of future successful performance."[25]

Global leadership requires a different set of attributes. At a Servant Leadership Research Roundtable, several scholars noted that global leaders now need several key attributes. They must be:

1. Open to other cultures and flexible.
2. Aware of verbal and nonverbal differences in communication with a person from another culture.
3. Aware that management practices developed in one culture may not be easily transferred to another.
4. Aware of the cultural influences on behavior.
5. Adaptive.
6. Loyal, honest, and ethical.
7. Have multidisciplinary perspectives, which are needed for problem solving.[26]

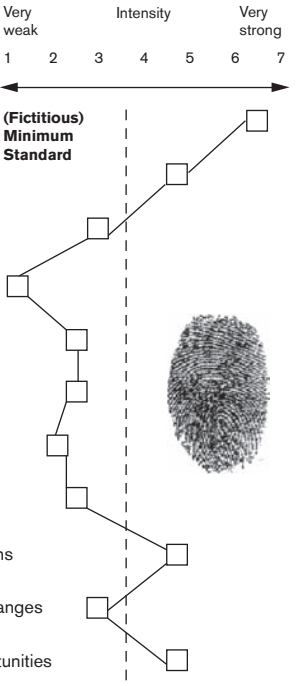
Although there are no definitive empirical or longitudinal studies that confirm skills of an ideal global manager or professional, research offers expertise areas for succeeding in international and global careers.[27] Figure 8.2 illustrates one such example. You will notice certain reoccurring competencies as you review these lists. Figure 8.3 extends the managerial competencies in Figure 8.2 with ethical dimensions of those skills. For example, having

Figure 8.2

Global Leadership Skills

How can the profit of an International manager be described?
Illustration of a Global Manager (fictional) Profile

- **Multidimensional perspective**
  Extensive multifunctional, multicountry, and multienvironment experience
- **Line management proficiency**
  Successful track record in overseas projects and assignments
- **Good decision making**
  Successful in making tactical and strategic decisions
- **Resourcefulness**
  Skilled in getting known and accepted by host country's stakeholders
- **Culturally sensitive**
  Can effectively deal with people from a variety of cultures
- **Culturally adaptive**
  Quick and easy to adapt to foreign culture; cross-cultural experiences
- **Team-building skills**
  Able to create culturally diverse working groups
- **Mental maturity**
  Endurance for the rigors of foreign posts (culture shock)
- **Negotiating skills**
  Track record of conducting successful (international) business negotiations
- **Change-agent skills**
  Track record of successfully initiating and implementing organizational changes
- **Visionary ability**
  Quick to spot and respond to political and economical threats and opportunities



Source: Based on Rainer Busch. (April 24, 2008). Global leadership skills. *RainerBusch.de.* http://www.rainerbusch.de/GLS-24-04-2008-Busch.pdf, accessed March 2, 2012.

a managerial "multidimensional perspective" (i.e., "Extensive multifunctional, multicountry and multienvironment experience") would be complemented by having a "multidimensional ethical perspective," which would in turn, as shown in Figure 8.2, require experience in managing cross-cultural country values and ethical orientations.

Another complementary list of global skills that are based on research and HR experience includes the following:[28]

- Strategic awareness
- Adaptability to new situations
- Sensitivity to different cultures
- Ability to work in international teams
- Language skills
- Understanding international marketing
- Relationship skills
- Family support
- International negotiating skills

Figure 8.3

Complementary, Managerial Ethical, and Social Responsibility Competencies

• **Multidimensional perspective** Extensive multifunctional, multicountry, and multienvironment experience	• **Multidimensional / ethical perspective** Multifunctional and multicountry business experience in leading with ethical values
• **Line-management proficiency** Successful track record in overseas projects and assignments	• **Line-management social responsibility** Socially responsible capacity in cross-cultural projects and assignments
• **Good decision making** Successful in making tactical and strategic decisions	• **Ethical decision making** Ability to negotiate ethically cross-culturally
• **Resourcefulness** Skilled in getting known and accepted by host country's stakeholders	• **Ethical resourcefulness** Skilled in getting known and accepted by host country's stakeholders for ethical reputation
• **Culturally sensitive** Can effectively deal with people from a variety of cultures	• **Cross-cultural ethics awareness** Can effectively communicate with others' cross-cultural values
• **Culturally adaptive** Quick and easy to adapt to foreign culture; cross-cultural experiences	• **Cross-cultural values adaptation** Quick and easy to adapt to different values while maintaining core ethical principles
• **Team-building skills** Able to create culturally diverse working groups	• **Team-building and social responsibility skills** Able to adapt to ethical differences of diverse working groups and relationships
• **Mental maturity** Endurance for the rigors of foreign posts (culture shock)	• **Moral maturity** Ability to work with rigors of different professionals' moral maturity
• **Negotiating skills** Track record of conducting successful (international) business negotiation	• **Negotiating skills across country cultures** Track record in successfully negotiating conflicting country norms and outcomes
• **Change-agent skills** Track record of successfully initiating and implementing organizational changes	• **Change-agent ethical skills** Track record of acting ethically in leading organizational change
• **Visionary ability** Quick to spot and respond to political and economic threats and opportunities	• **Stakeholder management skills** Quick to spot and respond to ethical issues in political and economic situations

Source: Based on Rainer Busch. (April 24, 2008). Global leadership skills. *RainerBusch.de.* http://www.rainerbusch.de/GLS-24-04-2008-Busch.pdf, accessed March 2, 2012. Adapted by Joseph W. Weiss, 2014. All rights reserved.

- Self-reliance
- Open, non-judgmental personality
- Flexibility of thinking
- Sensitivity to others
- Ability to see the "big picture"
- Leadership skills
- Drive and determination
- Intellectual capability

Many large companies outsource the assessment process for selecting managers and professionals to work abroad. Other firms have in-house assessment centers to evaluate, select, and train professionals for international and global work.

Shared Leadership in Teams' Competency

Recent research on workplace attitudes and values across 53 nations and regional groupings by professors at the Graduate School of Management in Claremont found that "teams that perform poorly tend to be dominated by the team leader, while high-performing teams have a shared-leadership structure. But beware: There are some risks executives run by sharing the reins. And our research suggests also that success may depend on the particular country where a business is operating."[29]

The researchers noted that it is more difficult to share leadership if members share values from a society that is based on unequal distribution of power. Those who occupy leadership positions are less likely to share their authority, since they likely believe it is something they have earned. Likewise, followers may be reluctant to share leadership because they view control as the sole prerogative of the appointed leader. Followers may also judge a leader to be weak if he or she attempts to hand over the reins. Countries, according to these researchers, where there is an unequal distribution of power include Arab countries, Belgium, Brazil, Chile, Colombia, Costa Rica, East Africa, Ecuador, France, Greece, Guatemala, Hong Kong, Indonesia, Iran, Korea, Malaysia, Mexico, Pakistan, the Philippines, Panama, Peru, Portugal, El Salvador, Singapore, Spain, Taiwan, Thailand, Turkey, Uruguay, West Africa, Venezuela, and Yugoslavia. Countries where power is more decentralized and that are more egalitarian include Argentina, Australia, Austria, Canada, Denmark, Finland, Germany, Britain, India, Ireland, Israel, Italy, Jamaica, Japan, the Netherlands, New Zealand, Norway, South Africa, Sweden, Switzerland, and the United States. Of course not every professional from a country in either of these two groupings shares that country's value system; this research is only an indicator. Use Ethical Insight 8.2 to find how you identify your preferences for team leadership, based on your country of origin as well as your beliefs about effective teams and leadership.

Ethical Insight 8.2

Country Culture Counts: Potential for Shared Leadership

Countries that accept unequal power distribution in organizations and institutions; centralized decision-making; inegalitarian: Arab countries, Belgium, Brazil, Chile, Colombia, Costa Rica, East Africa, Ecuador, France, Greece, Guatemala, Hong Kong, Indonesia, Iran, Korea, Malaysia, Mexico, Pakistan, the Philippines, Panama, Peru, Portugal, El Salvador, Singapore, Spain, Taiwan, Thailand, Turkey, Uruguay, West Africa, Venezuela, and Yugoslavia	Countries that do not accept unequal power distribution; decentralized decision making; egalitarian: Argentina, Australia, Austria, Canada, Denmark, Finland, Germany, Britain, India, Ireland, Israel, Italy, Jamaica, Japan, the Netherlands, New Zealand, Norway, South Africa, Sweden, Switzerland, and the United States

Questions

1. What is your country of origin? In which country have you lived, studied or worked the longest?
2. Which decision-making style do you prefer in a team: centralized or decentralized? Explain.
3. Which leadership decision-making style do you believe would allow for more ethical decisions: (a) centralized (single leader) or (b) decentralized (shared leadership)? Explain.
4. What has been your experience in observing how more ethically oriented teams have performed: those teams with centralized, authoritarian or decentralized, egalitarian leadership decisionmaking? Explain.

Source: Pearce, Craig. (July 7, 2008). Follow the leaders. *WSJ.com*. http://online.wsj.com/article/SB121441363110903891.html?mod=djem_jiewr_HR, accessed January 8, 2014.

Under the heading "Passing the Mantle," the Claremont researchers provide the following leadership insights:

- *The Mistake:* When companies put together teams of employees, they usually hamstring the group right from the start by appointing one team member to lead the crew.
- *The Alternative:* Leadership should be shared among team members, passing to whoever has the most expertise for the job at hand. Our research shows that when teams share leadership, their companies usually see big benefits.
- *The Caveat:* Shared leadership doesn't work in all situations—for instance, if the teammates haven't had time to learn each other's strengths and

gauge who should be in charge at any given time. Shared leadership also faces big hurdles in some cultures, such as those that generally favor strong central authority.[30]

To summarize, an individual's cultural background, based on country differences, can affect his/her effectiveness as a global team leader and member. Of course this type of difference is not the only factor determining team effectiveness, but being aware of the effects of others' and one's cultural background is important—not only for team membership but also for ethical decision-making differences, as we discussed earlier and will address again later in the chapter.

The final observation in this section is that HR experience indicates that "Fewer young people are willing to accept assignments overseas for fear their experience will not be recognized and they will encounter difficulties when coming back. It is therefore becoming critical for companies to select with precision and recruit the right personnel."[31] Other reasons new professionals hesitate to take overseas positions or long-term assignments include the following preconceptions about working away from the base of their company's operations: "nomadic and transient lifestyle; loss of ties to home and close friendships; [not knowing] how to integrate with local people; loss of usual support systems and people to turn to in an emergency; danger of terrorist activities and anti-western attitudes in some areas; and children's education and spouses' careers."[32] Companies must stress the positive opportunities for overseas careers, such as: "wider responsibility, often with greater freedom of action, enhanced quality of life, greater job satisfaction and, if successful, future career advancement, as well as opportunities to travel, to broaden horizons and possibly learn other languages."[33] We turn next to ethics from a global perspective.

Global Ethical Values and Principles

Because unethical practices cross geographic boundaries and affect nation-states as well as corporations doing business in different countries, there is a need for both legal regulation and ethical motivation. An example of a blatant illegal and unethical practice that has affected global business is South Africa's previous apartheid system that was supported by several local laws from 1948–1986. These laws condoned and even enforced racial segregation that protected white supremacy and domination. "Firms with subsidiaries operating in SA were bound by the apartheid legislation even though each of the laws could be ethically faulted."[34] Within that system, MNEs had to decide whether to continue supporting a system of racial discrimination and slavery by doing business in South Africa during that time, or leave. Other forms of questionable ethical behavior by different countries will be discussed later in this chapter, including: child labor, intolerable working conditions for employees, foreign firms paying below living wages for cheap labor, exporting proven hazardous products to different countries, and MNEs' usurping poorer

countries' environmental and natural resources to gain profit. For these reasons, global values and principles were developed by international agencies and institutions to inform and constrain all corporations doing business across national borders from illegal and unethical acts such as apartheid.

Examples of Global Principles and Values

There are different universal sets of values and ethical standards that are shared by MNEs. The Global Sullivan Principles are one such source. "These principles were developed by Leon Sullivan (the first African-American to be appointed to the board of a major corporation—General Motors) in 1977. General Motors was the largest American employer of black South Africans at the time."[35] Over 30 prestigious firms have agreed to these principles, which are shown in Table 8.1. Other such global codes, principles, and statements of universal rights include the Caux Round Table Principles for Business, the Amnesty International Human Rights Principles for Business, the Asian Pacific Economic Cooperation Forum Business Code of Conduct, the Ceres

Table 8.1
Global Sullivan Principles of Social Responsibility

The Principles
As a company which endorses the Global Sullivan Principles we will respect the law, and as a responsible member of society we will apply these Principles with integrity consistent with the legitimate role of business. We will develop and implement company policies, procedures, training and internal reporting structures to ensure commitment to these Principles throughout our organization. We believe the application of these Principles will achieve greater tolerance and better understanding among peoples, and advance the culture of peace. Accordingly, we will:
• Express our support for universal human rights and, particularly, those of our employees, the communities within which we operate, and parties with whom we do business.
• Promote equal opportunity for our employees at all levels of the company with respect to issues such as color, race, gender, age, ethnicity or religious beliefs, and operate without unacceptable worker treatment such as the exploitation of children, physical punishment, female abuse, involuntary servitude or other forms of abuse.
• Respect our employees' voluntary freedom of association.
• Compensate our employees to enable them to meet at least their basic needs and provide the opportunity to improve their skill and capability in order to raise their social and economic opportunities.
• Provide a safe and healthy workplace; protect human health and the environment; and promote sustainable development.
• Promote fair competition including respect for intellectual and other property rights, and not offer, pay or accept bribes.
• Work with governments and communities in which we do business to improve the quality of life in those communities–their educational, cultural, economic and social well-being–and seek to provide training and opportunities for workers from disadvantaged backgrounds.
• Promote the application of these Principles by those with whom we do business.

Source: Sullivan, The Rev. Leon H. The global Sullivan principles. *Mallenbaker.net.* http://www.mallenbaker.net/csr/CSRfiles/gsprinciples.html, accessed March 1, 2012.

Principles, the Clarkson Principles of Stakeholder Management, the International Labour Organization (ILO) Declaration of Fundamental Principles and Rights at Work, the Organisation for Economic Cooperation and Development (OECD) Guidelines for Corporate Governance, the OECD Guidelines for Multinational Enterprises, and the United Nations (UN) Declaration of Human Rights.

Guy's (1991) 10 core values also serve as a practical set of universal principles:[36]

1. Caring
2. Honesty
3. Accountability
4. Promise keeping
5. Pursuit of excellence
6. Loyalty
7. Fairness
8. Integrity
9. Respect for others
10. Responsible citizenship

Does One Set of Values "Fit" All?

Can one set of values apply to different cultures? Gilman and Lewis argued that universal "principles and common values are often—and wrongly—dismissed because actual behavior does not appear to coincide. . . . The apparent incoherence between expressed values and observed behavior does not make values irrelevant to cross-cultural comparisons."[37] The same authors cited empirical data from a study that included France, Germany, the United States, Japan, Mexico, South Africa, Argentina, Chile, Russia, Nigeria, and India to argue that although culture is a carrier of values, "values are not solely derived from one's culture."[38] In other words, there are universal principles and values that are not, nor should they be, culturally derived; rather, these principles should transcend cultures for the greater good of all. As we discuss in the last section of this chapter, issues emerge not only from the problem of identifying or agreeing on a set of universal ethical principles, but also when there is a clash between individuals, groups, and/or organizational interests that are constrained or denied by one or more of these principles. Doing the right thing may violate cultural norms in several cultures; some universal principles may take precedence over some cultural values for the common good, as well as for certain individual's and group's rights.

Know Your Own Cultural and Core Values, Your Organization's, and Those with Whom You Are Working

Corporate leaders and professionals working in different countries and globally need to know (1) their own cultural and ethical values and principles; (2) those of their organization or company; and (3) those of the individuals, team, and organization in whose culture they are working. Without this

knowledge, two particular "ethical traps" may face individual professionals, teams, and companies:

1. *Acting ethnocentrically* is demonstrating "the belief in the inherent superiority of one's own ethnic group or culture; a tendency to view alien groups or cultures from the perspective of one's own."[39] Acting from one's own cultural preferences without awareness of or concern for others' cultural values also has ethical consequences that can result in negative reactions from others and your failure to achieve business goals. Critics have accused the U.S. government of acting ethnocentrically in some of its policies and preemptive approaches to imposing democracy on some Middle Eastern countries. Some North American and European corporations in previous decades and empires have also acted ethnocentrically in their use and destruction of poorer countries' resources for competitive gain.

2. *Moral (and cultural) relativism* is based on "the view that no culture is superior to any other culture when comparing systems of morality, law, politics, etc. It's the philosophical notion that all cultural beliefs are equally valid and that truth itself is relative, depending on the cultural environment."[40] At a cultural level, acting from this theory involves "When in Rome, do as the Romans do"; or, do what your company believes is right at the time and in the immediate circumstance. If you had been working with an American company in South Africa in the 1970s, you may very well have been acting from this principle. You would have been, as noted earlier, accepting the practice of state-condoned racial discrimination. Some of the larger petroleum companies working in conjunction with other cohorts have been described as acting from a relativistic ethic to satisfy their own profits at the expense of the environment and poorer working peoples, who are barely surviving with increased energy and fuel prices.

A method you can use to understand your own cultural values and ethical principles—and those of your team and even organization—in an international setting is based on Harvard University's Joseph Badaracco's three key questions to consider before acting or taking a position in a "defining moment." His method is presented in Chapter 2; the following is an extension of that method.[41] We have added a cross-cultural dimension to the probes.

For individuals, the key question is "Who am I?" First, ask and discern "What cultural values, attitudes, and habits might influence my decision?" Second, what are my *ethical principles-in-action* (i.e., principles practiced): Do I generally rely on a utilitarian ethic? Do I rely on justice, fairness, and duty principles? Am I an altruist, pragmatist? Do I respect the rights of others? Or, do I make decisions based on relativism; that is, act from my own self-interest and cultural values only? Do I demonstrate virtues in my character and toward others? Also, am I flexible in my ethical thinking when dealing with others, or am I rigid and demanding? Third, with whom am I making this decision? Do I understand their basic cultural values? Do I know some of their ethical principles-in-action? With this understanding, you may then:

1. Identify your feelings and intuitions that are emphasized in the situation.
2. Identify your deepest values that are in conflict in the situation.
3. Consider the feeling and intuitions of the other(s) in the situation.
4. Identify what their values and ethics are and how these might affect the conflict in the situation.
5. Identify the best course of action to understand the right thing to do for you and the others.

In work groups, managers can ask, "Who are we?" (Again, consider each team member's cultural values as well as your own, and ask how the team reflects any particular set of values. Identify the ethical principles-in-action of the team). You can then address these three questions as a team in this situation:

1. What strong views and understanding of the situation do team members have—cross-culturally and within your own team?
2. Which position or view would most likely win over others in a way that would be least harmful culturally and organizationally to all affected?
3. Can we respond in this situation in a way that reveals the values we care about in this organization?

Company executives can ask, "Who is the company?" (What are its core values and ethical principles-in-action in this international context and global setting?) Three questions you can consider are:

1. Have I strengthened my position and the organization to the best of my ability, relying on my values and ethics?
2. Have I considered my organization's values and role vis-à-vis the society's (both my society's, and another's, if abroad) cultural values and interests in a bold and creative way?
3. How can I transform my vision based on these reflections into action that combines creativity, ethical responsibility, courage, and shrewdness?

As discussed in Chapter 2, these ways of reflecting on the contextual values and facts in a situation when a difficult decision must be made is not always easy, especially in a cross-national setting. Deciding between two or more positions that are culturally and even morally "right" for parties in conflict also requires moral courage, common sense, and shrewdness. Section 8.6 offers specific methods of negotiating conflicting values cross-culturally. Next, we discuss some ethical issues in business that professionals may encounter when working across national boundaries.

Cross-Cultural Business Ethical Issues Professionals May Experience

Some of the more predominant ethical issues that managers and professionals in international settings have experienced include (1) bribery and gifts, (2) sexual

and racial discrimination, and (3) piracy and intellectual property protection. These are a sample of such issues. The cases in this book present additional issues.

Bribery: A Form of Corruption

> A former senior manager at Siemens yesterday [May 26, 2008] admitted building up an elaborate system of slush funds and shell firms at the request of his superiors to help Europe's biggest technology group win overseas contracts through bribes. Reinhard Siekaczek told a Munich court that he had informed his entire divisional board about the system and assumed that the whole group executive board knew about it from at least 2004. On the opening day of Germany's biggest post-war corporate corruption trial, Siekaczek described how managers signed off "commissions" on yellow Post-It notes which could be easily removed in case of raids or investigations. His damning testimony included allegations that his efforts to stop the widespread bribery at Siemens' fixed-line telecommunications equipment division (Com), where he was a sales manager, had fallen foul of his superiors who "didn't want to hear." Siekaczek, aged 57, is the first of up to 300 accused among Siemens' current and former staff to stand trial in a corruption scandal that the group itself admits involves at least €1.3bn (£1bn) in siphoned-off money. Six of its divisions are involved in a bribery system spanning the globe that has so far cost it €1.8bn to clear up, including a €201m fine from another Munich court. It could result in a multibillion-dollar penalty from the U.S. Securities and Exchange Commission as well as the loss of lucrative contracts.[42]

Bribery can be a serious matter as the excerpt above shows. Bribery payments are estimated at $1 trillion worldwide.[43] Leaders' and professionals' careers can be lost, settlements and court costs can be substantial to companies, and reputations tarnished. Bribery is part of the definition of corruption ("Corruption: moral perversion, depravity, perversion of integrity, bribery, corrupt or dishonest proceedings, any corrupting influence or agency. Bribery: money or other valuable consideration given or promised with a view to corrupting the behavior of a person, a public official crime in some countries and not others").[44] Bribery is a global problem: "Bribery in developing countries often stems from multinationals based in the richest countries. Global financial centers play a role in allowing officials to move, hide and invest illicitly gained wealth. Principles and ethics vary between countries. Interestingly, the U.S. accepts domestic political or legislative influencing practices such as lobbying and campaign funding, while considering the same underlying activities corrupt in other countries. The responsibility to combat corruption is global and no country can hold itself above the solution."[45]

The organization Transparency International publishes a Buyers Payers Bribery Index, where a high average score indicates low bribery. The report shows a ranked list of the top 30 countries on bribery (note: China and India ranked last and are not shown on this short list). The top 15 in this Index are shown in Table 8.2.

Table 8.2
Rank / Country / Average Score (0–10)

1. Netherlands	8.8	9. United Kingdom	8.3
2. Switzerland	8.8	10. United States	8.1
3. Belgium	8.7	11. France	8.0
4. Germany	8.6	12. Spain	8.0
5. Japan	8.6	13. South Korea	7.9
6. Australia	8.5	14. Brazil	7.7
7. Canada	8.5	15. Hong Kong	7.6
8. Singapore	8.3		

Source: Transparency International. (2011). *Buyers payers index.* http://www.scribd.com/idunt/d/71267831-BPI-Report-Embargo-for-Viewing, accessed January 8, 2014.

International organizations that have addressed and ratified bribery in different countries' legislation include the OECD, the Organization of American States (OAS), and the Council of Europe (CoE).

In the United States, the Foreign Corrupt Practices Act (FCPA) was enacted in 1977 and substantially revised in 1988. The provisions of the FCPA prohibit the bribery of foreign government officials by U.S. persons and prescribe accounting and record-keeping practices that prohibit American companies from offering payments to foreign government officials for the purpose of obtaining or retaining business. "The fact that the FCPA deals only with bribes made to foreign government officials acts to exclude from the FCPA . . . payments to foreign persons who are not governmental officials. Additionally, the fact that the FCPA deals only with bribes that are intended for the purpose of obtaining or retaining business acts excludes grease or facilitating payments from the scope of the FCPA. A grease or facilitating payment is a payment made to expedite or secure the performance of a routine government action. Routine government actions include obtaining permits or licenses, processing official papers, clearing goods through Customs, loading and unloading cargo and providing police protection."[46] U.S. individuals who cannot defend their actions with regards to the FCPA's antibribery provisions can face harsh penalties. "U.S. companies can be fined up to $2 million while U.S. individuals (including officers and directors of companies that have willfully violated the FCPA) can be fined up to $100,000 and imprisoned for up to five years, or both. In addition, civil penalties may be imposed."[47]

Recently, the U.S. Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) have been more aggressive in enforcing and prosecuting the bribery section of the FCPA. Note the following example:

> In December 2007, Lucent agreed to settle parallel DOJ and SEC FCPA enforcement actions by paying $2.5 million in combined fines and penalties for improperly recording travel expenses and other things of value to employees of Chinese companies that were owned or controlled by the state (SOEs). Such individuals are deemed to be "foreign officials" under the FCPA's anti-bribery provisions.

> Pursuant to a DOJ non-prosecution agreement, Lucent acknowledged that from at least 2000 to 2003, it spent over $10 million on approximately 315 trips involving over 1,000 employees of Chinese SOEs that had a disproportionate amount of sightseeing, entertainment, and leisure. According to the government, while the trips Lucent paid for were "ostensibly designed to allow the Chinese foreign officials to inspect Lucent's factories and to train the officials in using Lucent's equipment . . . the officials spent little or no time in the United States visiting Lucent's facilities [but instead] visited tourist destinations throughout the United States, such as Hawaii, Las Vegas, the Grand Canyon, Niagara Falls, Disney World, Universal Studios, and New York."[48]

Also, the FCPA's penalties and levied fines have significantly grown in size. In December 2008, "the U.S. Department of Justice announced that the German conglomerate Siemens AG, along with its subsidiaries in Argentina, Bangladesh, and Venezuela, agreed to plead guilty to conspiring to commit violations of the U.S. Foreign Corrupt Practices Act (FCPA). The criminal fines imposed, totaling more than $450 million, are by far the largest in the history of the FCPA, and are supplemented by more than $350 million in ill-gotten profits."[49]

When doing business in developing countries where corruption, and particularly bribery, is prevalent, it is worth taking the following precautions:

- Read and understand the legislation and its enforcement on corruption and bribery in that country.
- Read and understand the FCPA and the OECD guidelines on corruption.
- Know your business associates and partners where you do business.
- Take an active role in education, compliance and due diligence.[50]

Gifts versus Bribery

A key question for new and even seasoned international business professionals is: When is a gift really a bribe? Peter Madsen, executive director of the Center for the Advancement of Applied Ethics and Political Philosophy at Carnegie Mellon University in Pittsburgh stated that "Hard and fast rules, however, tend to get blurry in international business settings. Even Fortune 500 companies with laudably firm policies have trouble in this area. . . . Relativism is rampant . . . and when you're talking business, cultural relativism becomes a really big problem."[51]

In most parts of the world, especially some less-developed nations, Asia, the Middle East, parts of Europe and the United States, business professionals are expected to "pay to play." Narayan Manandhar, former president of Transparency International in Nigeria, offered a distinction: "Personally, I like to see the bribe located at an intermediate position in a continuum where at one extreme you can put extortion and at the other, a gift. A bribe becomes extortion when it is demand-driven. If a medical doctor asks for a bribe inside an operation theater or an emergency room, it is clearly a matter of extortion.

You have been blackmailed to pay the bribe. A bribe could turn into a gift, if it is supply-driven. People have asked me whether tips paid to a waiter in a restaurant are a bribe or a gift. Normally, it is not a bribe. It is a gift as there is an element of voluntariness or the absence of a quid pro quo situation."[52]

The OECD uses the acronym GIFT, which expands as "(1) Genuine, (2) Independent, (3) Free, and (4) Transparent. First, the gift must be genuine, that is, offered in appreciation for something which you have done well, in accordance with your functions as a public official, without any encouragement. Second, the gift must be independent in a sense that it does not affect your functioning in the future. Third, it must be free from any obligations to the donor, or for his/her family or affiliates. Fourth, it must be transparent. You must be able to declare the gift in a completely transparent way, to your organization and its clients, to your professional colleagues, and to the media and the public in general."[53]

Racial and Sexual Discrimination in the Global Context

Two other areas in which professionals working globally are likely to experience ethical issues are racial and sexual discrimination. Although these issues and sexual harassment were discussed in Chapter 7, here we expand these topics to cross-cultural settings. "Discrimination is an assault on the very notion of human rights. Discrimination is the systematic denial of certain peoples' or groups' full human rights because of who they are or what they believe. International law guarantees human rights to all without distinction based on race, colour, sex, language, religion, political or other opinion, national or social origin, property, birth or other status. Governments are obliged to take essential measures to ensure the right of all to be free from discrimination," according to Amnesty International.[54] Globalization, the widening gap between income groups, the "global war on terror," and the post-9/11 environment have created opportunities and problems with regard to unintended consequences regarding racial discrimination. A brief sample of countries that have immigrant populations illustrates the potential for and experience with racial discrimination. The United States continues to deal with the need for labor while wrestling with "illegal immigration" from Mexico; England has one of the most diverse working populations in the world, with East Indian immigrants representing a large segment of that population; Germany must deal with integrating Turkish workers and immigrants; Dubai, the United Arab Emirates, and Saudi Arabia all import labor—of the 1.5 million residents of Dubai, 1 million are immigrants; "Argentina's population is 97 percent white (mostly of Spanish and Italian descent) and three percent mestizo (Amerindian and European). One of the difficulties in assessing and addressing persistent forms of racial discrimination in Argentina is the lack of adequate information about the population, particularly the indigenous and immigrant communities."[55] Racial discrimination doesn't only occur between native residents and immigrants of host countries. As noted above, discrimination is practiced in different forms including in MNEs as well as with an international labor force. Racial discrimination here refers to the

workplace and generally involves acts relating to hiring, wage inequalities, treatment of employees, working conditions, and promotions.

A world survey on workplace discrimination shows the disparity in opinions about racial discrimination and also calls on governments to act to prevent such acts:[56]

- Majorities in 15 out of 16 nations [polled] agree that employers do not have the right to discriminate. Asked whether employers should be allowed to "refuse to hire a qualified person because of the person's race or ethnicity," on average three out of four (75%) say employers should not be able to base hiring decisions on race, while just 19% believe they should.
- Majorities against workplace discrimination are largest in France (94%), China (88%), the United States (86%), Indonesia (84%), Britain (83%), and Azerbaijan (82%).
- Again, India stands apart from the other countries polled. Although a plurality opposed such discrimination, an unusually high 30% says that employers should be allowed to reject jobseekers because of race or ethnicity. Relatively large minorities also agree that employers should be free to hire whom they choose in Nigeria (34%) and South Korea (41%), though in both cases, majorities are opposed (64% and 58%, respectively).
- Indonesians (80%) and the Chinese (77%) believe overwhelmingly that the government should try to prevent discriminatory hiring practices, followed by Azerbaijanis (72%), the French (69%), Americans (69%), Britons (69%), Ukrainians (65%), Mexicans (64%), and Iranians (61%). More modest majorities agree in Russia (58%), Egypt (56%), Nigeria (56%), the Palestinian territories (53%), and South Korea (53%).
- Two countries differ: Turkey and India. Only 23% of Turks say that the government has the responsibility to take measures against workplace discrimination and 43% say it does not. Among Indians, just 27% say that government has this responsibility, while 20% say it does not.

Companies hiring and integrating employees into their firms benefit from having corporate leaders and cultures that do not tolerate racial discrimination. Lack of respect and fairness from employers in their hiring, promotion, and reward practices leads to employee turnover, absenteeism, and lower performance. Employees usually turn first to their supervisors in the chain of command to report or discuss discrimination problems. If the company has no formal or written policy, the employee must decide whether or not to pursue the issue to others in the organization or go outside. Corporations can benefit from establishing such policies and procedures along with training to support their workforce.

The UN Human Rights Council moved to establish a new subsidiary body, the Expert Mechanism on the Rights of Indigenous Peoples, on December 13, 2007. Other UN agencies, nongovernmental organizations (NGOs), and different countries' human rights groups, such as the European Commission

against Racism and Intolerance (ECRI), which was established by the first Summit of Heads of State and Government of the Council of Europe Member States, all continue to implement policies, help create laws, and monitor racial discrimination not only in workplaces but also in different societies. Companies moving to different countries and those already serving different countries need to familiarize their officers and professionals with the work of these UN bodies and NGOs. Many large, established MNEs have partnered and worked with such bodies for decades.

Sexual Discrimination

Sexual discrimination is generally part of laws dealing with other types of discrimination and rights, such as race, age, national origin, gender, religion, and language. Not all countries have laws or even policies dealing with sexual harassment and/or discrimination specifically against women, or men. In a cross-national survey published in 2000, France, Germany, Mexico, the Philippines, Switzerland, Taiwan, and Venezuela had no "prohibitions on employment discrimination." Several countries also had no "prohibitions on sexual harassment" in the workplace—Ukraine, Singapore, Russia, Republic of South Africa, Poland, China, Hungary, Czech Republic, Colombia, and Brazil. Note that "In Europe, there is an increasing focus on behaviors described as 'moral harassment,' 'mobbing,' or 'workplace bullying,' all of which subordinate concern about the integration of women in the workforce to concern about the rights of all workers."[57]

Companies working globally that follow universal principles and values will adopt sexual harassment and discrimination policies and be clear that women are included in such policies. Since leadership and professional talent in many regions of the world is at record shortages, companies cannot afford to exclude the protection of competent women leaders and professionals from these policies: "Laws that protect workers from sexual harassment conceive of sexual harassment in a number of different ways: as discrimination based on sex, as an offense against dignity, or as an issue of health and safety in the workplace. The discrimination conception of sexual harassment law reflects an understanding that such law is designed to protect a vulnerable group—in this case mainly women—that is the target of inappropriate sexual behavior in the workplace. From this viewpoint, laws prohibiting sexual harassment must be implemented so as to remove an obstacle to the integration of women in the workforce. . . . Many countries have adopted the anti-discrimination model of sexual harassment law in an attempt to protect the rights of women in the workplace."[58]

Piracy and Intellectual Property Protection

Intellectual property (IP) is best defined in the context of a quote from a U.S. Trade Representative: "Innovation is the lifeblood of a dynamic economy here in the United States, and around the world. We must defend ideas, inventions and creativity from rip off artists and thieves."[59] When any materials or products are patented, trademarked, and copyrighted in the United States or other countries, these items are assumed to be protected under law. Brands

are valuable commodities. When imitated, copied, and abused, the owners and originators of the brand are harmed.

IP theft is estimated at $250 billion annually, according to the U.S. Commerce Department. The Internet Crime Complaint Center recorded 303,809 complaints in 2010 alone.[60]

Illegal file-sharing of music has been facilitated by the Internet and has become a practice of global piracy. That debate is ongoing. However, when countries protect or do not punish piracy of IP, the issue moves to a different level and can involve government-to-government and global issues. For example: "The threat to IP from backroom thieves who produce counterfeit and pirated products is absolutely the most pervasive threat to the global economy as a whole. The U.S. Chamber of Commerce estimates that counterfeiting and pirated products account for 5 to 7 percent of the global economy, costing the United States alone over 750,000 jobs, and socks U.S. industry for a loss of sales in the area of $250 billion. The Chamber has directed its efforts, via trade missions and educational programs, toward China, Brazil, South Korea, and Russia with the goal of encouraging enhanced enforcement of IP protection laws within."[61]

China, Russia, Argentina, Chile, Egypt, India, Israel, Lebanon, Thailand, Turkey, Ukraine, and Venezuela are countries on the priority list that is monitored by the United States for intellectual piracy. The Bahamas, Bulgaria, Croatia, the EU, and Latvia have been removed from the watch list. Intellectual piracy between countries is also viewed in the context of trading agreements and how countries adopt stricter laws to prevent, decrease, and stop observed violations.

Gupta and Wang take a more entrepreneurial view of IP piracy. They state that even if over 80% of the software and music consumed in China and India is pirated, the estimated piracy rates in the United States are at about 30%. Also the governments of China and India are becoming serious about laws enforcing IP; their motivation is to accelerate their country's science and technology base. The authors note that "Instead of obsessing about these issues, companies should aim for a rapid rate of innovation that makes life difficult for imitators and pirates in developed and developing countries alike. Rapid innovation may not reduce piracy, but it will help ensure that pirates' products are viewed as consistently inferior, and thus less desirable." They continue: "Companies can also reduce piracy by making their products or services more affordable. This is what Microsoft is now attempting with the introduction of Windows XP Starter Edition, a no-frills and low-priced version of its operating system for India, Brazil and many other emerging markets." U.S. and international firms could reduce IP leakage "by dispersing R&D and production across China, India and other locations."[62]

Companies operating in other countries where IP violations are prevalent need to have clearly stated policies and procedures that are communicated and supported with training to those employees who are responsible for handling these issues with the firm's stakeholders.

8.3 Societal Issues and Globalization: The Dark Side

At a larger societal level, it is difficult to determine whether the process of globalization is the cause or effect of the forces driving this phenomenon. Certainly governments, MNEs, and transnational corporations (TNCs) affect this process, but they too are influenced by the forces driving the changes. In this section, we discuss some of the broader "dark side" issues of globalization before discussing the role of MNEs. The process of globalization may be producing "losers"; that is, countries that cannot share in the wealth- and health-generating processes, activities, and outcomes of globalization because they are either excluded from or ignored with respect to the positive side of globalization, including technology development and use, education, and economic development. However, many of the issues discussed here are being addressed by UN agencies, NGOs, and country governments. Corporations and strategic alliances are attacking problems with the natural environment, as discussed in previous chapters.

Critics generally argue that globalization has caused, or at least enhanced, the following problems: crime and corruption; drug consumption; pollution of the environment; massive layoffs that occur when companies move to regions that offer cheaper labor; decreases in wages; the erosion of individual nations' sovereignty; and the Westernization (led by Americanization) of culture, standards, and trends in entertainment, fashion, food, technology, ways of living, and values. These are not all of the issues related and attributed to globalization, but they are substantial ones that also affect the economies and populations that comprise the environments in which businesses operate.

International Crime and Corruption

"In Eastern Europe, traffickers ship girls through the Balkans and into sex slavery. Russians launder money through tiny Pacific islands that have hundreds of banks but scarcely any roads. Colombian drug barons accumulate such vast resources that they can acquire a Soviet submarine to ship cocaine to the United States. . . . It is clear that the globalization of crime is a logical outcome of the fall of Communism. Capitalism and Communism, ideologies that served as intellectual straitjackets for Americans and Soviets, allowed them to feel justified in unsavory proxies to fight their cold war."[63] The *Global Trends 2015* report estimates that corruption costs $500 billion annually, equivalent to 1% of the global economy. The report also stated that in the illegitimate economy, narcotics trafficking has projected annual revenues of $100–$300 billion. Auto theft in Europe and the United States is estimated to net $9 billion, and the sex slave business projects $7 billion. Every third cigarette exported is sold on the black market.[64] The Corruption Perception Index (CPI)—based on the perceptions of ordinary citizens, business leaders, and experts and developed by the nonprofit group Transparency International—shows that the most corrupt countries in 2012 were Somalia, North Korea, Afghanistan, Sudan, Myanmar, Uzbekistan, Turkmenistan, Iraq, Venezuela, and Haiti. The United States ranked as the 19th least corrupt

Figure 8.4

Ranking of Countries' Public Sector Corruption According to the 2013 Corruption Perceptions Index

Least "Corrupt"			Most "Corrupt"		
Rank	Country	Score	Rank	Country	Score
1	Denmark	91	157	Zimbabwe	21
1	New Zealand	91	160	Cambodia	20
3	Finland	89	160	Eritrea	20
3	Sweden	89	160	Venezuela	20
5	Norway	86	163	Chad	19
5	Singapore	86	163	Equatorial Guinea	19
7	Switzerland	85	163	Guinea-Bissau	19
8	Netherlands	83	163	Haiti	19
9	Australia	81	167	Yemen	18
9	Canada	81	168	Syria	17
11	Luxembourg	80	168	Turkmenistan	17
12	Germany	78	168	Uzbekistan	17
12	Iceland	78	171	Iraq	16
14	United Kingdom	76	172	Libya	15
15	Barbados	75	173	South Sudan	14
15	Belgium	75	174	Sudan	11
15	Hong Kong	75	175	Afghanistan	8
18	Japan	74	175	Korea (North)	8
19	United States	73	175	Somalia	8
19	Uruguay	73			
21	Ireland	72			
22	Bahamas	71			

Note: A country/territory's score indicates the perceived level of public sector corruption on a scale of 0-100, where 0 means that a country is perceived as highly corrupt and 100 means that a country is perceived as very clean. A country's rank indicates its position relative to the other countries/territories included in the index. Burundi and Myanmar share the 157th position with a score of 21.

Source: From the 2013 Transparency International's Corruption Perceptions Index. http://www.transparency.org/whatwedo/pub/cpi_2013. This index measures the perceived level of public-sector corruption in countries and territories around the world. © Transparency International 2013. All Rights Reserved. Reprinted with permission.

country. See Figure 8.4 for recent survey results of the global CPI. It is interesting to note that some of the industrialist leading nations did not rank at the top for noncorrupt activities.

Economic Poverty and Child Slave Labor

Child labor rates are slowing down. Since 2000, the number of children working as child laborers has declined from 246 million to 168 million, 85 million of whom still work in hazardous conditions (ILO-IPEC, 2013).[65] An exception is in Sub-Saharan Africa, where child labor is increasing. Most child laborers continue to work in agriculture. Only one in five are paid. The overwhelming majority are unpaid family workers.[66] Child labor among girls has fallen by 40% since 2000, compared to 25% for boys. Child labor exists in both developing and industrialized countries, but mostly in South and Southeast Asia, South America, Africa, and increasingly in Eastern Europe, where there is an economic transition from a command economy to a market economy.[67]

Globalization has bypassed Africa; in Sub-Saharan Africa illiteracy is high and modern infrastructure (telecommunications, reliable electrical power) do not exist.[68] The gap in per capita gross domestic product (GDP) between the richest and poorest countries in the world is about 140:1. This gap will increase as the shift from industrial- to knowledge-based economies continues to occur. Third World countries must modernize around new technologies in order to gain the benefits of globalization.[69]

Some regions of the Ivory Coast continue to attract child-labor traffickers (those who buy, enslave, and sell children to work on industrial projects and plantations, like cocoa and chocolate production). Annual wages paid for children under the age of 14 are about U.S. $135 to U.S. $165.[70]

The Third World includes not only all of Sub-Saharan Africa, but also large parts of the Middle East and much of South Asia and Central and South America. "Hunger is common; disease is rampant; infant mortality is high; life expectancy is short."[71] Notable economists from the Group of Eight (leading industrial countries) conclude that solutions to Third World poverty must include "systematic attempts to change incentives at every level in the global system—from the gangsterish Third World governments that exploit their citizens to the international institutions that prop them up through continued lending."[72]

The Global Digital Divide

Article 19 of the International Covenant on Civil and Political Rights (1966) states that "Everyone shall have the right to freedom of expression; this right shall include freedom to seek, receive and impart information."[73] "The term Digital Divide refers to the gap between individuals, households, businesses and geographic areas at different socio-economic levels with regard to both their opportunities to access information and communication technologies (ICTs) and their use of the Internet for a wide variety of activities." Currently,

"70% of the world population is still excluded from the use of information technologies."[74]

As of 2011, "the digital divide is growing wider across the world as broadband access becomes out of reach for many in emerging markets." Research by analysts Richard Hurst and those at Ovum showed that broadband costs are significantly greater for those in emerging countries. "According to a survey of 19 emerging markets, it was found that some countries are charging over triple what developed nations have to shell out for what is increasingly seen as a basic human right. In South Africa, for instance, entry level services went as high as $1,443 per year, with high end services reaching an enormous $6,000."[75]

Ventures are under way to provide poorer children with computers. Nicholas Negoponte at MIT started the nonprofit One Laptop Per Child (OLPC) organization that was set up to develop and market a low-cost (under $100) education-focused laptop for the poorest children across the globe. Another venture is Bill Gates' Microsoft research lab in India, where he is focusing on projects that provide "low-cost wireless to new computing interfaces that will allow semi-literate and illiterate people to use computers effectively."[76] Still, one-third of the world's population is disconnected from and has no access to the Internet. This fact continues to broaden the divide between the haves and the have-nots and between the First and Third World countries. Less than 1% of online users live in Africa. Less than 5% of computers are connected to the Internet in developing countries. The developed world has almost 50 phone lines for every 100 people, compared to 1.4 phones per 100 people in low-income countries. Countries excluded from the global economy are those that cannot and do not build access to the Internet. Wireless technologies offer encouraging signs for Third World country access to First World technologies.[77] The EU has committed to concentrate its efforts on formulating information on society policies, focusing on EU coordination, Internet governance, and financing.[78] The United States, technology MNEs, and other regional alliances are also working to fund and supply less-advantaged countries with Internet capabilities.[79]

Westernization (Americanization) of Cultures

Globalization has brought "Americanization" (some critics say American imperialism) to other cultures through fast-food commerce (McDonald's, the *Fast Food Nation,* and *Food, Inc.* phenomenon discussed in Chapter 5). The "McDonaldization of Society,"[80] as noted in Chapter 5, is "the process by which the principles of the fast-food restaurant are coming to dominate more and more sectors of American society as well as the rest of the world."[81] George Ritzer, the author of the book *The McDonaldization of Society*, argues that "McDonaldization affects not only the restaurant business but also education, work, the criminal justice system, health care, travel, leisure, dieting, politics, the family, religion, and virtually every other aspect of society."[82] (Ritzer states toward the end of his book that "McDonaldization will some-

day pass on when the nature of society has changed so dramatically that they can no longer adapt to it."[83])

In addition to fast food, the Internet has brought instant exposure to all forms of American culture: entertainment, films, news, music, and art. Values and ways of living underlie these influences and are not always welcome in many countries—France, China, Singapore, and countries in the Middle East to name a few. Serious ethical questions are asked that are related to problems and threats of globalization through Westernization: "Does globalization result in cultural and economic homogenization through a heightened emphasis on consumerism? Do local and global values change as a result of international integration that promotes the conversion of national economies into environmentally and socially harmful export-oriented systems for competition in geographically and culturally transcendent 'world markets'?"[84]

American-based advertising to children, in particular, also has come under criticism in the United States. Juliet Schor's book, *Born to Buy* (2004), examines American contemporary culture, in which advertising significantly affects children aged 18 months through 13 years. Schor's research shows that children shopped "50% more than the preceding generation, both with their parents and on their own. The supermarket was the predominant consumer arena. . . . Commodities have become increasingly influential especially in social dynamics within schools."[85]

Children's advertising also affects foods children eat, clothes they buy, product brands they know and select when shopping, advice on relationships with parents and friends, and what they watch on TV and in the cinema. According to Schor, one remedy of this process would be the "decommercialization of food, media space, and the outdoors." She advocates for a "national comprehensive curriculum in gardening, menu planning, eco-literacy, and science and nutrition."[86] The point here is that American advertising—like entertainment, media, and films—is becoming another export that carries habits and a way of life that other cultures may find unacceptable.

Loss of Nation-State Sovereignty

Critics also protest that globalization erodes the ability of governments to protect the interests of their citizens against more powerful MNEs. At conflict are the benefits of economic globalization and the laws and institutions within these nations' own boundaries. Part of the debate centers on the argument that market forces are global and must be dealt with by global businesses.

There is also tension over sovereignty between nations and MNEs regarding power and influence. An example was the rejection of the proposed merger between General Electric (GE) and Honeywell by the European Commission's antitrust authorities. That merger, it was argued, would have left public interest behind, because these companies bring different legal and regulatory traditions across the Atlantic. Opinions differed among American and European antitrust officials as to GE's dominant market position. Other mergers blocked by the EU include: Deutsche Telekom and Beta Research;

Volvo and Scania; and MCI WorldCom and Sprint.[87] On the other hand, Microsoft's fine by the EU on monopoly charges indicates that the global environment is a playing level where international law applies.[88]

Loss of nation-state arguments diminish when evidence is provided that MNEs cannot, and do not claim to, protect citizens during wars and regional conflicts; collect taxes; distribute benefits; build roads and infrastructure; care for the environment; or protect the rights of individuals, groups, and the elderly. In fact, governments subsidize and support companies when needed. In the immediate aftermath of the terrorist attack on the World Trade Center, the U.S. airlines suffered sizable financial losses. It is estimated that 2007–2008 losses in the industry were $6.1 billion.[89]

Other industries (e.g., railroad, automobile, agribusiness, aerospace) have also been subsidized by government funds. Still, it is argued that "globalization will continue to chip away at the power of the nation state. As the Europeans know from their experience over the last 50 years, surrendering some degree of national autonomy is a natural and inevitable concomitant of growing economic interdependence."[90] The degree to which nation-states share and/or give up power, influence, and sovereignty to global companies—and the types of power, influence, and sovereignty they do give up or share—is and will be a continuing subject of debate.

8.4 Multinational Enterprises as Stakeholders

An MNE or TNC is generally regarded as "an enterprise comprising entities in more than one country which operate under a system of decision-making that permits coherent policies and a common strategy. The entities are so linked, by ownership or otherwise, that one or more of them may be able to exercise a significant influence over the others and, in particular, to share knowledge, resources and responsibilities with the others."[91] MNEs and TNCs are corporations that "own or control production or service facilities outside the country in which they are based."[92] Companies go global to enhance profit by creating value, building and increasing markets, and reducing costs. Costs are reduced by locating and using raw materials, skilled labor, land, and taxes at lower costs. Value can also be added by joint-venturing with other national and regional partners who have market reach, global skills, experience, and resources.

A 2012 *Harvard Business Review* article notes an interesting trend: the role of MNEs in the U.S. economy has been declining. Most U.S. MNEs have been expanded faster overseas; however, MNEs still accounted for 75% of the labor productivity growth in the United States from 1977 to 2000. About half of the new job growth of MNEs came from Brazil, Russia, India, and China (or the "BRICs"). "Leaders of global corporations are voicing concerns about a deep set of U.S. challenges—complex taxation, inadequate worker skills, crumbling infrastructure—that inhibit hiring and investment in America. In contrast, corporate leaders see dynamic opportunities in countries like China and India."[93]

Power of MNEs

Although MNEs often reflect and extend their home nation's culture and resources, many are powerful enough to act as independent nations. This section focuses on MNEs as independent, powerful stakeholders, using their power across national boundaries to gain comparative advantages, with or without the support of their home country. The following facts indicate the power of MNEs:[94]

- Worldwide employment by U.S. MNEs decreased to 33.4 million workers in 2008. Employment in the United States by U.S. parent companies decreased to 22.9 million workers. The employment by U.S. parents accounted for almost one-fifth of total U.S. employment in private industries. Employment abroad by the majority-owned foreign affiliates of U.S. MNEs increased 1.7%, to 10.5 million workers.
- Worldwide capital expenditures by U.S. MNEs increased 4.1% in 2008, to $708.2 billion. Capital expenditures in the United States by U.S. parents increased 2.3%, to $519.7 billion. Capital expenditures abroad by majority-owned foreign affiliates increased 9.1%, to $188.5 billion.
- Sales by U.S. parent companies increased 3.2% in 2008, to $9,509.0 billion. Sales by majority-owned foreign affiliates increased 10.9%, to $5,520.2 billion.

The world's largest companies are shown in Figure 8.5. They include Wal-Mart, Royal Dutch Shell, ExxonMobil, BP, Sinopec Group, China National Petroleum, State Grid, Toyota Motor, Japan Post Holdings, and Chevron. Of the 500 largest corporations, 133 are U.S. firms, 68 are Japanese, and 35 are French.

The dominant goal of MNEs is, as noted earlier, to make a profit and take comparative advantage of marketing, trade, cost, investment, labor, and other factors. At the same time, MNEs assist local economies in many ways, as is explained below. The ethical questions critics of MNEs have raised are partly reflected in the following statement by the late Raymond Vernon, noted Harvard professor and international business expert: "Is the multinational enterprise undermining the capacity of nations to work for the welfare of their people? Is the multinational enterprise being used by a dominant power as a means of penetrating and controlling the economies of other countries?"[95] The next subsection addresses these questions in a discussion of the mutual responsibilities and expectations of MNEs and their host countries.

Misuses of MNE Power

Corporations cannot act as if they operate in a social vacuum. Society's values changed after September 11, 2001, and in order to maintain legitimacy, organizations are now expected to take into consideration a new social framework where society expects them to go beyond mere financial decisions and do "the right thing." This change is evident from the hundreds of shareholder resolutions, lodged in recent years, relating to social issues. It is also reflected

Figure 8.5

World's Largest Companies

Search Rank	Company	Revenues ($b)	Profits ($b)
1	Royal Dutch Shell	481.7	26.6
2	Wal-Mart Stores	469.2	17.0
3	ExxonMobil	449.9	44.9
4	Sinopec Group	428.2	8.2
5	China National Petroleum	408.6	18.2
6	BP	388.3	11.6
7	State Grid	298.4	12.3
8	Toyota Motor	265.7	11.6
9	Volkswagen	247.6	27.9
10	Total	234.3	13.7

Sources: *CNNMoney.com.* (2013). Global 500: Our annual ranking of the world's largest corporations. http://money.cnn.com/magazines/fortune/global500/2013/full_list/?iid=G500_sp_full, accessed October 6, 2013; DeCarlo, S. (April, 17, 2013). The world's biggest companies. *Forbes.com.* http://www.forbes.com/sites/scottdecarlo/2013/04/17/the-worlds-biggest-companies-2/, accessed June, 2013; PWC. (2013–2014). Global top 100 companies–the risers and fallers. http://www.pwc.com/gx/en/audit-services/capital-market/publications/top100-market-capitalisation.jhtml, accessed August, 2013.

in the new environment of corporate social responsibility and increased disclosure. The stream of corporate failures, the subprime lending crisis, and the fragility of the U.S., European, and global financial systems have led to critics questioning more closely the motives and many practices of MNEs and large corporations' management in general.[96] From an ethical perspective, we ask: Why are some MNEs not paying their fair share of taxes in countries where they are located? Why are MNEs pushing their costs of doing business on to taxpayers and the public? Why are MNEs not treating the environment as a public good instead of as a "negative externality"; that is, as a "spillover" cost from businesses to third parties? Why are MNEs not treating and paying local labor better in less developing—and even some developed—countries? Why are some markets treated less equally and equitably—for example, why do some pharmaceuticals not put the same warning labels on drugs in poorer, less regulated markets as they do in more developed, richer countries? Why are children and women in some developing countries discriminated against in labor practices by some MNEs? Of course, not all MNEs violate international law or take advantage of less-developed countries' markets and peoples; however, our interest here is discussing ways in which MNEs operate (and have operated) in host countries, in order to explore more socially responsible practices.

Crises since the birth of the MNE after World War II have raised international concern over the ethical conduct of MNEs in host and other countries.

Not long ago, the Ford-Bridgestone/Firestone tire crisis was international in nature. These companies were not forthright early on with their consumers about defects known by the companies. Union Carbide's historic chemical spill disaster in Bhopal, India, resulted in thousands of deaths and injuries and alarmed other nations over the questionable safety standards and controls of MNE foreign operations. Nestlé's marketing of its powdered infant milk formula that resulted in the illness and death of a large number of infants in less developed countries raised questions about the lack of proper product instructions issued to indigent, less-educated consumers. (Nestlé's practice resulted in a boycott of the company from 1976 to 1984.)

The presence of MNEs in apartheid-era South Africa raised criticisms over the role of large corporations in actively supporting apartheid or government-supported racism. Because MNEs had to pay taxes to the South African government and because apartheid was a government-supported policy, MNEs—it is argued—supported racism. Several U.S.-based MNEs that operated in South Africa witnessed boycotts and disinvestments by many shareholders. Many MNEs, including IBM and Polaroid, later withdrew. Post-apartheid South Africa has seen the reentry of companies from all countries. Another long-standing moral issue is the practice of MNEs of not paying their fair share of taxes in countries where they do business and in their home countries. Through transfer pricing and other creative accounting techniques, many MNEs have shown paper losses, thereby enabling them to avoid paying any taxes.

Critics claim that many MNEs are not fulfilling their part of the implicit social contract discussed in Chapters 4 and 5. Some of these critics include Richard Barnet and John Cavanagh in their book *Global Dreams,* David Korten in *When Corporations Rule the World,* Tom Athanasiou in *Divided Planet: The Ecology of Rich and Poor,* Paul Hawken in *The Ecology of Commerce,* and William Greider in *One World, Ready or Not.*[97] MNEs' practices subject to criticism include committing corporate crimes, exerting undue political influence and control, determining and controlling plant closings and layoffs, and damaging the physical environment and human health. Evidence regarding these claims showed, for example, that 11% of 1,043 MNEs studied were involved in one or more major crimes over a 10-year period. The crimes included foreign bribery, kickbacks, and improper payments. A small sample of those firms included Enron, WorldCom, Adelphia, American Cyanamid, Anheuser-Busch, Bethlehem Steel, Allied Chemical, Ashland Oil, and Beatrice Foods.[98]

Large corporations (along with trial lawyers and labor unions) also have immense influence through political action committees (PACs). The organization Common Cause noted that the majority of soft money contributions to both American parties in 1999 came from corporate business interests. With regard to plant closings and "downsizings," critics are concerned that some MNEs are more concerned with a particular profit margin than with their share of responsibility to community and society. After all, taxpayers support roads and other external conditions that allow corporations to operate in a country. Although corporations are not expected to be a welfare system for employees, critics note that large companies are expected to share in the social

consequences of their actions, especially when, for example, plant-closing decisions are made to reap the benefits of cheaper labor in another country.

Finally, there is historical evidence that several large corporations have harmed the physical environment and the health of their employees and local communities. Classic crises cases discussed in Chapter 5 regarding asbestos manufacturing, oil spills, chemical plant explosions, toxic dumping, and industrial air pollution demonstrate corporate misuses of the environment in recent history. The external and human costs that communities, governments, the environment, and taxpayers have had to pay for these misuses of power have been documented.

In the following sections, two perspectives regarding global corporations' responsibilities—that of the MNE and that of the host country—are discussed.

MNE Perspective

"A rising tide lifts all ships." MNEs enter foreign countries primarily to make profit, but they also create opportunities host countries would not have access to without these companies. Although MNEs benefit from international currency fluctuations, available labor at cheaper costs, tax and trade incentives, the use of natural resources, and gain access to more foreign markets, these companies benefit their host countries through foreign direct investment and in these ways:

- Hire local labor.
- Create new jobs.
- Co-venture with local entrepreneurs and companies.
- Attract local capital to projects.
- Provide for and enhance technology transfer.
- Develop particular industry sectors.
- Provide business learning and skills.
- Increase industrial output and productivity.
- Help decrease the country's debt and improve its balance of payments and standard of living.

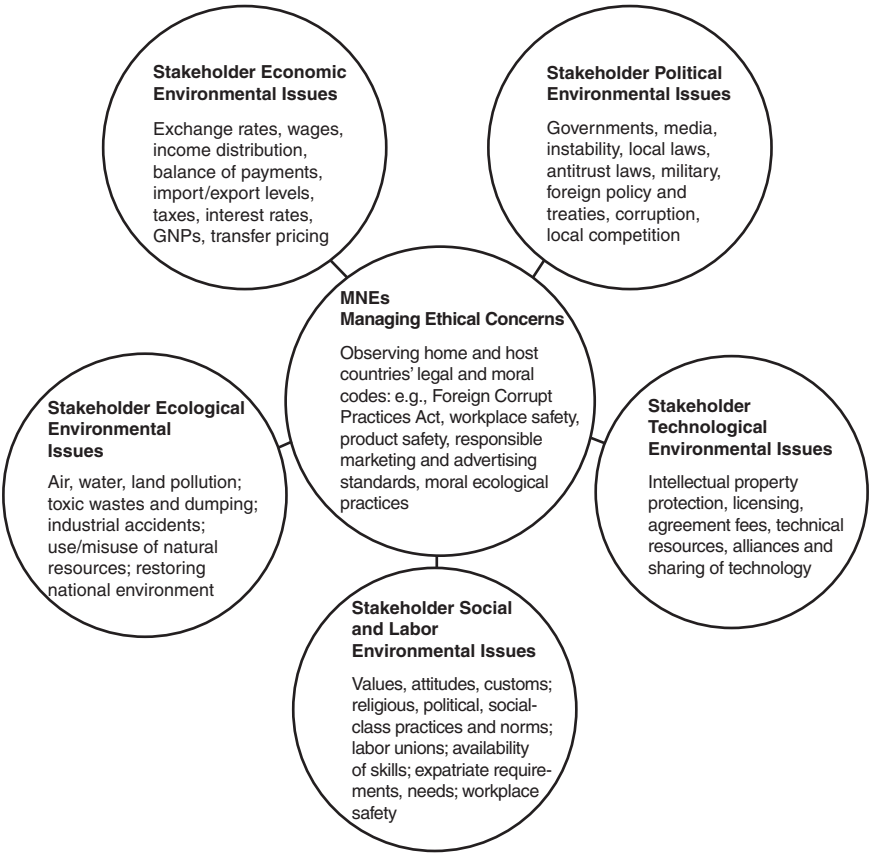
Moreover, MNEs open less-developed countries (LDCs) to international markets, thereby helping the local economy attract greatly desired hard currencies. Also, new technical and managerial skills are brought in, and local workers receive training and knowledge. Job and social-class mobility is provided to inhabitants.[99] Some MNEs also establish schools, colleges, and hospitals in their host countries. For example, although Nike has been criticized for its international child labor practices, it is also true that by contracting with factories abroad, it has helped employ more than half a million workers in 55 countries. Eighty-three percent of Nike's workforce in Indonesia are women who would not otherwise be employed.[100] Another company, Patagonia, Inc., has given 1% of its annual sales to environmental groups and gives employees up to two paid months off to work for nonprofit environmental

groups. The company also routinely permits independent human rights organizations to audit any of its facilities and participates in the Apparel Industry Partnership (AIP) to set standards to expose and monitor inhumane business practices in their industry. Cadbury is another example of a company that has practiced highly ethical standards abroad. In India, the company hired local workers and instilled new work-related ethical values in its plant.[101]

The MNE must manage overlapping and often conflicting multiple constituencies in its home- and host-country operations. Figure 8.6 illustrates some of the major environmental and stakeholder issues the MNE must technically and ethically balance and manage in its foreign location. From the MNE's perspective, managing these stakeholder issues is difficult and challenging, especially as the global economy presents new problems.

Figure 8.6

MNE Global Stakeholder Management Issues and Ethical Concerns



Source: Copyright © Joseph W. Weiss, Bentley University, Waltham, MA. 2014.

MNE executives and other managers also complain of what they consider unethical practices and arbitrary control by host-country governments. For example, local governments can and sometimes do the following:

- Limit repatriation of MNE assets and earnings.
- Pressure and require MNEs to buy component parts and other materials from local suppliers.
- Require MNEs to use local nationals in upper-level management positions.
- Require MNEs to produce and sell selected products in order to enter the country.
- Limit imports and pressure exports.
- Require a certain amount or percentage of profit to remain in or be invested in the country.

Finally, MNEs can face the threat of expropriation or nationalization of their operations by the host government. More recently, MNEs must assume high-stakes risks, liabilities, and responsibilities in the area of safety, especially since September 11. The airline industry in particular, has been hit very hard by this unpredictable crisis. The crisis itself, along with the "fallout" over laxness in safety standards and enforcement, has taken a heavy toll on all U.S. and most international carriers. The price of doing business safely has escalated.

Host-Country Perspective

Six criticisms of the presence and practices of MNEs in host and other foreign locations are discussed here.

1. MNEs can dominate and protect their core technology and research and development (R&D), thus keeping the host country a consumer, not a partner or producer. The Brazilian government, for example, has counteracted this by having entry barriers and laws that, since the 1970s, have protected against the complete control of its own electronics industries by foreign manufacturers. It is also argued (or feared) that Japan's MNEs could in the long term dominate certain critical industries (such as the electronics industry and perhaps the automobile industry) in the United States and use American labor more as assemblers than as technology R&D partners.
2. MNEs can destabilize national sovereignty by limiting a country's access to critical capital and resources, thereby creating a host-country dependency on the MNE's governments and politics.
3. MNEs can create a "brain drain" by attracting scientists, expertise, and talent from the host country.
4. MNEs can create an imbalance of capital outflows over inflows. They produce but emphasize exports over imports in the host country, thereby leaving local economies dependent on foreign control.
5. MNEs can disturb local government economic planning and business practices by exerting control over the development and capitalization

of a country's infrastructure. Also, by providing higher wages and better working conditions, MNEs influence and change a country's traditions, values, and customs. "Cultural imperialism" is imported through business practices.

6. MNEs can destroy, pollute, and endanger host-country and LDC environments and the health of local populations. For example, the mining of and dangerous exposure to asbestos continue in some LDCs and in Canada.

Obviously, these criticisms do not apply to all MNEs. These criticisms represent the concerns of host-country and LDC governments that have suffered abuses from MNEs over the decades. Tensions in the relationships between MNEs and host countries and other foreign governments will continue, especially in the least-developed settings. Whenever the stakes for both parties are high, so will be the pressures to negotiate the most profitable and equitable benefits for each stakeholder. Often, it is the less-educated, indigent inhabitants of LDCs who suffer the most from the operations of MNEs.

More global companies are beginning to self-monitor and contribute to host-country education, consumer awareness, and community programs (e.g., Shell has written a primer on human rights with Amnesty International; Hewlett-Packard offers consumer education programs and computer training in host countries).

8.5 Triple Bottom Line, Social Entrepreneurship, and Microfinancing

Positive trends in large and small businesses (globally and locally) include the "triple bottom line" philosophy and practices, social entrepreneurship, and microfinancing. These movements and practices are based on related premises and have in common a theme that serving society and the environment is also profitable. These are not new trends, but they are becoming more popular and acceptable ways of doing business, given the social, environmental, and moral problems businesses have and are experiencing at the expense of societies worldwide.

The Triple Bottom Line

The triple bottom line is "a kind of balanced scorecard that captures in numbers and words the degree to which any company is or is not creating value for its shareholders and for society."[102] This philosophy is based on "the sustainability imperative"; that is, the realization that in order for the environment to be preserved and society to benefit from business, corporations must respect the "interdependence of various elements in society on one another on the social fabric. Sustainability means operating a business in a way that acknowledges the needs and interests of other parties . . . and that does not

fray but rather reinforces the network of relationships that ties them together."[103] The triple elements of this scorecard argue that business activity should be measured in economic, environmental, and social costs and benefits. The economic dimension includes: sales, profits, return on investment (ROI), taxes paid, monetary flows, and jobs created; the environmental dimension includes air and water quality, energy usage, and waste produced; and the social dimension includes labor practices, community impacts, human rights, and product responsibility. "The sustainability sweet spot" where "increase profits and market share" and "address climate change and public health" intersect, indicates where a corporation's profits can be made. This has been demonstrated in several companies such as Tropicana's and Quaker Oats' healthy products, PepsiCo's environmental policy and procedures changes, Toyota's hybrid cars, and GE's clean technology ("ecomagination") products.

Social Entrepreneurs and Social Enterprises

A social enterprise is "an organization or venture that advances its social mission through entrepreneurial, earned income strategies."[104] Social entrepreneurs "are individuals with innovative solutions to society's most pressing social problems. They are ambitious and persistent, tackling major social issues and offering new ideas for wide-scale change. Rather than leaving societal needs to the government or business sectors, social entrepreneurs find what is not working and solve the problem by changing the system, spreading the solution, and persuading entire societies to take new leaps."[105] Social entrepreneurship and enterprises date back to the 1960s and 1970s and include nonprofits, community groups, youth social entrepreneurial groups, as well as the private and governmental sectors.[106] Some NGOs are also related to social enterprises. In 2008, *Fast Company* magazine's Social Capitalist Awards honored 45 social entrepreneurs "who are changing the world."[107]

Microfinancing

This related movement is making a difference for the poor globally.[108] Microfinancing involves "very small loans, typically less than $100 . . . made to the rural poor in developing countries who normally do not qualify for traditional banking credit. This is often the only way they can establish a business and lift themselves out of poverty."[109] Microfinancing is the idea of Professor Yunus, who in 1976 founded the Grameen Bank after a famine in Bangladesh. In 2008, the bank had 6.6 million borrowers, of whom 97% were women. The Nobel Peace Prize was awarded to Yunus and his Grameen bank in 2006 for this practice. "Grameen, which means village, is an idea that has spread to more than 40 countries including Sri Lanka where women's banks were already a familiar concept."[110]

8.6 MNEs: Stakeholder Values, Guidelines, and Codes for Managing Ethically

Guidelines for managing international ethical conduct have received detailed attention and effort over the past four decades in the areas of consumer protection, employment, environmental pollution, human rights, and political conduct.[111] Figure 8.6 illustrates issues and ethical concerns that MNEs must manage. The driving institutional forces behind the development of global ethical values, published guidelines, and universal rights include the UN, the ILO, the OECD, the Ceres Principles, the Conference Board, and the Caux Round Table Principles for Business.

The underlying normative sources of the guidelines that these global organizations have developed include beliefs in (1) national sovereignty, (2) social equity, (3) market integrity, and (4) human rights and fundamental freedoms.[112] Richard DeGeorge specifically offers the following guidelines that MNEs can use in dealing with LDCs:

1. Do no intentional harm.
2. Produce more good than harm for the host country.
3. Contribute to the host country's development.
4. Respect the human rights of their employees.
5. Respect the local culture; work with, not against, it.
6. Pay their fair share of taxes.
7. Cooperate with the local government to develop and enforce just background institutions.
8. Majority control of a firm includes the ethical responsibility of attending to the actions and failures of the firm.
9. Multinationals that build hazardous plants are obliged to ensure that the plants are safe and operated safely.
10. Multinationals are responsible for redesigning the transfer of hazardous technologies so that such technologies can be safely administered in host countries.[113]

Other developments involving global companies and business ethics include the following: (1) global companies are, as discussed earlier, developing and using core principles relevant to their business practices; (2) codes of ethics with minimum social responsibility standards (e.g., gender discrimination and environmental responsibility) are being adopted and employees are being trained on them; and (3) a broad consensus for ethical requirements is being articulated. The Conference Board, a global network of businesses, academic institutions, governments, and NGOs in more than 60 countries, is working to define global business practice standards, core principles for doing business across cultures, and the requirements for the support of and cooperation between business and nonbusiness institutions.[114]

Some classic guidelines that continue to influence policies and practices of global companies are presented next. The following MNE guidelines are summarized under the categories of employment practices and policies, consumer

protection, environmental protection, political payments and involvement, and basic human rights and fundamental freedoms.[115]

Employment Practices and Policies

- MNEs should not contravene the workforce policies of host nations.
- MNEs should respect the right of employees to join trade unions and to bargain collectively.
- MNEs should develop nondiscriminatory employment policies and promote equal job opportunities.
- MNEs should provide equal pay for equal work.
- MNEs should give advance notice of changes in operations, especially plant closings, and mitigate the adverse effects of these changes.
- MNEs should provide favorable work conditions, limited working hours, holidays with pay, and protection against unemployment.
- MNEs should promote job stability and job security, avoiding arbitrary dismissals and providing severance pay for those unemployed.
- MNEs should respect local host-country job standards and upgrade the local labor force through training.
- MNEs should adopt adequate health and safety standards for employees and grant them the right to know about job-related health hazards.
- MNEs should, minimally, pay basic living wages to employees.
- MNEs' operations should benefit the low-income groups of the host nation.
- MNEs should balance job opportunities, work conditions, job training, and living conditions among migrant workers and host-country nationals.

Consumer Protection

The following two items summarize best ethical and socially responsible practices for protecting consumers in a host country:

- MNEs should respect host-country laws and policies regarding the protection of consumers.
- MNEs should safeguard the health and safety of consumers by various disclosures, safe packaging, proper labeling, and accurate advertising.

Environmental Protection

The following items summarize best ethical and socially responsible practices for protecting a host country's environment:

- MNEs should respect host-country laws, goals, and priorities concerning protection of the environment.

- MNEs should preserve ecological balance, protect the environment, adopt preventive measures to avoid environmental harm, and rehabilitate environments damaged by operations.
- MNEs should disclose likely environmental harms and minimize the risks of accidents that could cause environmental damage.
- MNEs should promote the development of international environmental standards.
- MNEs should control specific operations that contribute to the pollution of air, water, and soils.
- MNEs should develop and use technology that can monitor, protect, and enhance the environment.

Political Payments and Involvement

Two basic, foundational cautions that argue against MNE's taking, giving, or being involved in any way with bribes and illegal payments and related politics with host country representatives:

- MNEs should not pay bribes or make improper payments to public officials.
- MNEs should avoid improper or illegal involvement or interference in the internal politics of host countries.

Basic Human Rights and Fundamental Freedoms

The following items broadly summarize the general principles underlying universal human rights and fundamental freedoms of all people that should be observed by MNEs:

- MNEs should respect the rights of all persons to life, liberty, security of person, and privacy.
- MNEs should respect the rights of all persons to equal protection of the law, to work, to choice of job, to just and favorable work conditions, and to protection against unemployment and discrimination.
- MNEs should respect each person's freedom of thought, conscience, religion, opinion and expression, communication, peaceful assembly and association, and movement and residence within each state.
- MNEs should promote a standard of living to support the health and well-being of workers and their families.
- MNEs should promote special care and assistance to motherhood and childhood.

William Frederick states that these guidelines should be viewed as a "collective phenomenon," because all do not appear in each of the five international pacts they originated from: the 1948 UN Universal Declaration of

Human Rights, the 1975 Helsinki Final Act, the 1976 OECD Guidelines for Multinational Enterprises, the 1977 ILO Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy, and the 1972 UN Code of Conduct on Transnational Corporations.[116] The guidelines serve as broad bases that all international corporations use to design specific policies and procedures; these corporations can then apply their own policies and procedures to such areas as "child care, minimum wages, hours of work, employee training and education, adequate housing and health care, pollution control efforts, advertising and marketing activities, severance pay, privacy of employees and consumers, and information concerning on-the-job hazards."[117]

8.7 Cross-Cultural Ethical Decision Making and Negotiation Methods

"You are a manager of Ben & Jerry's in Russia. One day you discover that the most senior officer of your company's Russian venture has been 'borrowing' equipment from the company and using it in his other business ventures. When you confront him, the Russian partner defends his actions. After all, as a part owner of both companies, isn't he entitled to share in the equipment?"[118] These and so many other international business situations confront managers and professionals with dilemmas and gray areas in their decision making. As one author noted, "Global business ethics has now become the ultimate dilemma for many U.S. businesses."[119]

"Transnationals operate in what may be called the margins of morality because the historical, cultural, and governmental mores of the world's nation-states are not uniform. There is a gray area of ethical judgment where standards of the transnational's home country differ substantially from those of the host country. . . . There is yet no fixed, institutionalized policing agency to regularly constrain morally questionable practices of transnational commerce. Moreover, there is no true global consensus on what is morally questionable."[120] Scholars and business leaders agree that solving ethical dilemmas that involve global, cross-cultural dimensions is not easy. Often there are no "quick fixes." Where other laws, business practices, and local norms conflict, the decision makers must decide, using their own business and value judgments. Ethics codes help, but decision makers must also take local and their own company's interests into consideration. In short, there is no one best method to solve international business ethical dilemmas. From a larger perspective, external human rights and corporate monitoring groups are also needed to inform and advise corporations before dilemmas occur about human rights and methods that can prevent abuses of local workers and private citizens.

External Corporate Monitoring Groups

Corporations and their leaders are ultimately responsible for articulating, modeling, and working with international stakeholders to enforce legal and

ethical standards in their firms as they do business around the world. Many do. However, as noted earlier, gray areas and lack of universal laws and norms leave loopholes that companies and local groups might use as competitive, but harmful, cost-saving advantages (e.g., not providing even "living wages" to the poor women and children they employ, polluting the environment, and using undue political influence to beat out competition). Numerous international groups that work with and monitor MNEs regarding human rights include—but are not limited to—Amnesty International (promotes and advocates human rights), OECD (developed guidelines for MNEs), ILO (publishes and works in the area of human rights), NGOs (combat corruption, assure adequate labor conditions, and establish standards for economic responsibility), Transparency International (monitors and publishes the international Corruption Perception Index), Apparel Industry Partnership (which develops codes of conduct regarding child labor practices and working conditions related to "sweat shops" and subcontractors), and the Caux Round Table (an executive group formed in Switzerland that published the noted Caux Principles and works with other international business professionals on developing and implementing universal ethics codes).[121] These groups work with, and some are composed of, MNE executives, governments, legislators, local citizenry, and other stakeholders worldwide to inform, monitor, and assist MNEs with ethical global business practices. Sandra Waddock states that

> Demands for greater corporate transparency and accountability, as well as anti-corruption measures are fostering significant new accountability, reporting, and transparency initiatives among coalitions of business, labor, human rights, investor, and governmental bodies. . . . A database created by the International Labor Organization and available over the Internet lists nearly 450 web sites of industry and business associations, corporate, NGO and activist groups, and consulting organizations that have developed and are promulgating a wide range of relevant policy initiatives. These initiatives include a mix of transparency and reporting initiatives, codes of conduct, principles, and fair trade agreements. Responses to these demands are varied. Many companies, particularly those under NGO and social activist pressures to reform labor and human rights abuses in their supply chains, have formulated their own codes of conduct. Notable among these companies are Levi-Strauss, Nike, and Reebok, all significant targets of activism.[122]

In the following section, several guidelines are discussed to complement principles and "quick tests" presented in Chapter 2.

Individual Stakeholder Methods for Ethical Decision Making

> In an international environment, the temptations can be strong, and the laws looser, or less obvious. Pressure from headquarters to make the bottom line can also weigh heavily. "Sometimes people confuse norms with ethics—exploitation of child labour, bribery and kickbacks may be the norm, but that doesn't mean

> they're right—and that's what companies need to deal with," says Joseph Reitz, who is co-director of the International Center for Ethics in Business at the University of Kansas. "There's lots of evidence that companies insisting on doing business in the right way may suffer in the short term, but in the long run they do well."[123]

Or do they? When confronted with cross-cultural ethical dilemmas, conflicting norms, and potentially illegal acts in international situations, individual employee and professional stakeholders need guidelines. Professionals and executives preparing to work abroad should ask for country-specific training on regional and local laws, customs, and business practices. As noted earlier, these professionals need to know their own firm's acceptable and unacceptable policies and procedures regarding negotiations and business dealings. This section introduces some—but obviously not all—guidelines that are a beginning step to becoming aware of the cultural differences and potential ethical consequences of doing business in other regions and countries.

DeGeorge offers the following general tactics that serve as a basic start for preventing, as well as solving, ethical dilemmas internationally:[124]

1. Do not violate the very norms and values that you want to preserve and that you use to evaluate your adversary's actions as being unethical. Seek to pursue with integrity economic survival and self-defense tactics. Winning a tactical battle unethically or illegally is not the goal.

2. Use your moral imagination, because there are no specific rules for responding to an ethical opponent. Stakeholder analysis can help. Explore different options. Use literature, stories, and lives of heroes and saints for creative responses instead of rules.

3. Use restraint and rely on those to whom the use of force is legitimately allocated when your response to immorality involves justifiable force or retaliation. Use minimal force that is justified as the ultimate solution, realizing that force is a reaction to unethical acts and practices.

4. Apply the principle of proportionality when measuring your response to an unethical opponent. The force you use should be commensurate with the offense, the harm suffered, and the good to be gained.

5. Use the technique of *ethical displacement* when responding to unethical forces. This principle consists of searching for clarification and a solution to a dilemma on different, higher levels than the personal (e.g., as discussed in Chapter 1, look at the problems from these levels: international, industry, organizational, structural, and national or legislative policy).

6. Use publicity to respond to an unethical practice, adversary, or system. Corruption, unethical and illegal practices and actions, operates best in the dark. Using publicity judiciously can mobilize pressures against the perpetrators.

7. Work jointly with others to create new social, legal, or popular structures and institutions to respond to immoral opponents.

8. Act with moral courage and from your values, personally and corporately.

9. Be prepared to pay a price, even a high one. Innocent people sometimes must pay costs that others impose on them by their unethical and illegal activities.

10. Use the principle of accountability when responding to an unethical activity. Those who harm others must be held accountable for their acts.

Getting to Yes

Solving a moral dilemma in an international context is not easy. Roger Fisher, Bruce Patton, and William Ury's *Getting to Yes: Negotiating Agreement Without Giving In* (alluded to earlier in this text) remains a classic primer for negotiating. Their four-step approach includes:

1. Separate the people from the problem.
2. Focus on interests, not on positions.
3. Insist on objective criteria, never yield to pressure.
4. Invent options for mutual gain.

The authors note that it is always necessary to determine your best alternative to a negotiated solution before starting a negotiation.[125]

Building on Fisher, Patton, and Ury's method, Nancy Adler states that formal negotiations, especially in an international or cross-cultural context, proceed through four stages after preparing for a negotiation:

1. Build interpersonal relationships (learn about the people)—separate people from the problem.
2. Exchange task-related information—focus on interests, not positions.
3. Persuade—invent options for mutual gain, instead of relying on preconceived positions, high pressure, or "dirty tricks."
4. Make concessions and agreements—use objective decision criteria.[126]

Understand the Local Culture First

Is local culture important or are people across cultures becoming more alike, especially with globalization and for those working in MNEs? Studies show that although organizations are becoming more alike in their structures and technologies, individuals maintain and even emphasize their cultural behaviors even more. National culture explains more about employees' attitudes and behaviors than does age, gender, role, or race.[127] When communicating and negotiating in different cultural contexts, gaining an understanding of the local culture in preparing for the negotiation is recommended before using any specific negotiation technique. Cultural miscues and disconnects are grounds for creating and exacerbating ethical problems and dilemmas. Consider, then, these cultural differences before problem solving or negotiating with counterparts:

- What are the dominant, underlying values of the culture? (Are groups, families, and collectives and their decisions valued over individuals and individual decisions, or vice versa?)

- How formally or informally are relationships viewed? (Is it necessary to get to know someone before negotiating, or is jumping to the facts first acceptable?)
- How do people understand and value rules versus spontaneity and bending rules? (Do friendships come before rules or are rules seen as unbreakable and applicable to all?)
- How are authority and power viewed? (Is position and status valued more than experience? Is the boss more often seen as being right regardless of "the facts"?)
- Is age respected as indicating wisdom and authority?
- To what extent does the culture avoid or embrace uncertainty and risk? (Are people threatened by ambiguity and therefore avoiding unpredictability?)

Sources that address these and other comparative cultural differences are readily available.[128]

Figure 8.7 illustrates different negotiating strategies among North Americans, Japanese, Chinese, and Latin Americans, based on cultural values and characteristics. Can you see how ethical problems and dilemmas could arise from communication miscues among professionals from these countries negotiating a complex transaction?

Figure 8.7

Four Typical Styles of International Ethical Decision-Making Negotiating Strategies with American, Japanese, Chinese, and Brazilian Cultures

American Negotiators	Japanese Negotiators	Chinese (Taiwanese) Negotiators	Brazilian Negotiators
Preparation and planning skill	Dedication to job	Persistence and determination	Preparation and planning skill
Thinking under pressure	Perceive and exploit power	Win respect and confidence	Thinking under pressure
Judgment and intelligence	Win respect and confidence	Preparation and planning skill	Judgment and intelligence
Verbal expressiveness	Integrity	Product knowledge	Verbal expressiveness
Product knowledge	Demonstrate listening skill	Interesting	Product knowledge
Perceive and exploit power	Broad perspective	Judgment and intelligence	Perceive and exploit power
Integrity	Verbal expressiveness		Competitiveness

Source: LeBaron, M. (July 2003). Culture-based negotiation styles. *BeyondIntractability.org.* http://www.beyondintractability.org/essay/culture_negotiation/, accessed January 10, 2014.

It is helpful to understand how other cultures perceive, understand, and perhaps even stereotype American cultural characteristics. (Obviously, not everyone from every culture reflects all of his/her national culture's characteristics.) For example, characteristics most commonly associated with Americans from the different nationals reveal interesting patterns (e.g., although Americans were largely seen as industrious, inventive, intelligent, decisive, and friendly by an interview sample of French, Japanese, Western Germans, British, Brazilians, and Mexicans, Americans were also seen as nationalistic, rude, and self-indulgent by Japanese; sophisticated by western Germans; nationalistic by Brazilians; and greedy by Mexicans).[129] Becoming self-aware of one's cultural characteristics (attitudes, values, behaviors, and others' perceptions of us) is an important step toward business transactions in order to prevent and negotiate ethical dilemmas.

Four Typical Styles of International Ethical Decision Making

At a more macro level, George Enderle identified four distinctive international ethical decision-making styles that companies often use when making decisions abroad: (1) Foreign Country style: a company applies the values and norms of its local host—"When in Rome, do as the Romans do"; (2) Empire style: a company applies its own domestic values and rules; this can be an imperialistic practice; (3) Interconnection style: a company applies shared norms with other companies and groups; national identities and interests are transcended and blurred, as when states make commercial decisions and rely on North American Free Trade Agreement (NAFTA) or the EU members to offer agreed-on processes and solutions; and (4) Global style: a company abstracts all local and regional differences and norms, coming up with a more cosmopolitan set of standards and solutions for its actions in the host country.[130]

The Foreign Country and Empire styles have obvious drawbacks in reaching ethical decisions. The Foreign Country style may result in gross injustices and inequities that are inherent in the norms adopted. Some local country norms and business practices, for example, do not prohibit child labor. The Empire style is a form of imperialism that disregards local norms and practices. The Global style, seemingly the "right answer," also presents problems. This style imposes its own interpretation of a "global morality and truth" on a host culture and norms. The Global style can also suffer from shortcomings shared by the Foreign Country and Empire styles. The Interconnection style "acknowledges both universal moral limits and the ability of communities to set moral standards of their own. It balances better than the other types a need to retain local identity with the acknowledgment of values that transcend individual communities. The drawbacks of this style are practical rather than moral." Companies and individual employees usually do not have quick or direct access to a commonly shared local, national, and international source to advise on a particular issue. Of the four styles, the Interconnection style appears to be less arbitrary and absolutist.[131] Another option is creative ethical navigation (which Thomas Donaldson and Thomas Dunfee term

"integrative social contracts theory" [ISCT]). This is not really a "style" of decision making; rather, it is the process of a decision maker navigating among "hypernorms," company interests, and local norms, as explained in the following section.

Hypernorms, Local Norms, and Creative Ethical Navigation

It would be helpful to have a set of norms that everyone agreed on. Hypernorms represent such an ideal. "Hypernorms are principles so fundamental that, by definition, they serve to evaluate lower-order norms, reaching to the root of what is ethical for humanity. They represent norms by which all others are to be judged."[132] Hypernorms relate to universal rights: for example, the right not to be enslaved, the right to have physical security, the right not to be tortured, and the right not to be discriminated against.[133] However, the problem even with hypernorms is that when "rights," local traditions, country economic systems, or business practices conflict, decisions have to be made; in such cases, it is necessary for a manager or professional to use his or her hypernorms as a starting principle, but then to be creative in considering the local context and competing norms. Reaching a win–win situation without violating anyone's norms is an ideal goal. An example of such a troublesome gray area, along with a suitable solution, is offered by Donaldson and Dunfee:

> Consider another situation confronted by Levi-Strauss, this time involving hypernorms connected with child labor. The company discovered in the early 1990s that two of its suppliers in Bangladesh were employing children under the age of fourteen—a practice that violated the company's principles but was tolerated in Bangladesh. Forcing the suppliers to fire the children would not have insured that the children received an education, and it would have caused serious hardship for the families depending on the children's wages. In a creative arrangement, the suppliers agreed to pay the children's regular wages while they attended school and to offer each child a job at age fifteen. Levi-Strauss, in turn, agreed to pay the children's tuition and provide books and uniforms. This approach allowed Levi-Strauss to uphold its principles and provide long-term benefits to the host country.[134]

Donaldson and Dunfee's "Global Values Map" illustrates conflicting local-country versus foreign-company norms and values that can clash when negotiating business contracts across cultures. The challenge for both local-country business professionals and foreign-country-company business professionals is to creatively navigate among value and norm differences to reach agreement on acceptable business practices.[135] Donaldson and Dunfee introduce "hypernorms," which are universal values acceptable to all cultures and organizations. "Consistent norms" are culture-specific values but are still consistent with both hypernorms and other legitimate norms. Ethical codes of companies, such as Johnson & Johnson's Credo (see Chapter 6), are examples of consistent norms. When a "foreign-company" representative's norms clash

with a host-country business individual's local norms, each must seek "moral free space" to negotiate value and norm differences. Both parties can encounter inconsistent norms when each holds to their own values and preferences, which may conflict with hypernorms and/or local business practices. Either party can experience illegitimate norms—values or practices that transgress hypernorms (e.g., exposing workers to asbestos or other carcinogens)—when negotiating individual business interests. In the "moral free space," a company and host-country professional can explore how to reach a negotiated deal that satisfies both their values and norms, while each gives up certain practices to do so. The above example of Levi Strauss illustrates such a negotiating process when Levi Strauss had to decide among a "hypernorm" (child labor is wrong), while embracing its own company norms ("consistent norms"—children cannot be hired or used by company suppliers). At the same time, Bangladesh suppliers' endorsed child-labor practices ("illegitimate norms" from Levi Strauss' perspective). An agreement had to be reached that would benefit the children and their families and the Bangladesh suppliers. The company and the Bangladesh suppliers, each desiring and needing the benefits of a negotiated contract, entered the "moral free space" and worked out what seems to have been a win–win situation for all parties involved—and an arrangement that brought no harm to any party.

Finding such creative solutions to international moral dilemmas involves balancing and combining business pressures, legal enforcement, and political will. A company attempting to make tough decisions with local groups could also seek to do so with the cooperation of other companies, local government officials, or even an external human rights group, as the Interconnectedness style of decision making would suggest. The ultimate decision may very well entail no compromise after reflecting on the situation, the hypernorm, and a company norm. Still, the methods discussed here can enable a decision maker—individual or global or company team—to look for options without getting trapped into blind absolutes, amoral gray zones, or relativism. Entering "moral free space" requires flexibility and negotiating.

Chapter Summary

The global environment consists of MNEs managing a dynamic set of relationships among country governments, international organizations, and each other. Elements of those relationships consist of financial markets, cultures, political ideologies, government policies, technologies, and laws. There are estimates of between 40,000 to 100,000 MNEs doing business across national boundaries and contributing to the global economy. It is likely these numbers will increase. Also, emerging markets in countries referred to as the BRICs (Brazil, Russia, India, and China) have and are helping to reshape the global landscape. New and competitive opportunities created by information technologies and the "flattening" of boundaries through the emergence of global supply chains, outsourcing, and China's "cost innovation" business model abound through mass production.

Globalization is the integration of technology, markets, politics, cultures, labor, production, and commerce. Globalization is both the process and the result of this integration. The global economy is estimated at $33 trillion. As the complexity and volatility of the global environment increases, the probability of ethical dilemmas and conflicts is also enhanced. The post-9/11 world has also created different constraints and costs on business and nations: the economic, legal, moral, and social pressures businesses face have several industries continuing to struggle for survival and profitability.

Forces that have accelerated globalization include the end of communism and the opening of closed economies; information technologies and the Internet, which accelerate communication and productivity within and across companies globally; entrepreneurship and entrepreneurs who are more mobile, skilled, intelligent, and thriving worldwide; free trade and trading agreements among nations; the flow of money through the World Bank and the IMF, which offers a conduit to bring needed capital to countries participating in building the global economy; the growth and the spread of transnational firms, which open new markets and create local employment; and a shift to service economies and educating workers using technologies, which has also propelled innovation and productivity worldwide. A question commonly asked is: Will globalization and accelerated business integration across national borders be slowed or rejuvenated through new and changing business, governmental, and entrepreneurial alliances, including ongoing corruption and "bubbles" bursting in different national economies felt around the world?

The "dark side" of globalization includes such issues as corporate crime and corruption, child slave labor, Westernization (Americanization) of values, the global digital divide, and loss of nation-state sovereignty. Also, critics argue that the "McDonaldization of Society" delivers cultural values as well as fast food. This is a debatable issue and was discussed in the chapter.

The power of MNEs, or global companies, lies in their size, economic prowess, and ability to locate and operate across national borders. MNEs offer benefits to their host countries by employing local populations, investing capital, co-venturing with local entrepreneurs and companies, providing enhanced technology, developing particular industry sectors, providing business learning and skills, and increasing industrial output and productivity.

MNEs also abuse their power by committing corporate crimes, exerting undue political influence and control, determining and controlling plant closings and layoffs, and damaging the physical environment and human health. Guidelines drawn from more than four decades of international agreements and charters were summarized to illustrate a consensus of host-country rights that have been used to help MNEs to design equity into their policies and procedures.

Finally, principles from *Getting to Yes: Negotiating Agreement Without Giving In* were extended to include understanding cross-cultural characteristics of decision makers to prevent ethical dilemmas and negotiate complex business transactions. A creative model was summarized enabling companies to

reach agreements among conflicting hypernorms (universal rights), consistent norms (company ethics and values codes), and illegitimate norms. Being able to balance local cultural norms, a company's norms, and competing business practices involves creative and responsible navigation and decision-making skills based on personal, professional, company, and universal values.

Questions

1. Briefly characterize the emerging competitive global business environment and identify some of the forces that define it.
2. What is "globalization"? What are some of the forces driving this process?
3. What competencies do you (a) have, and (b) need if you were to join–or are already working for–a global company in which you would spend time in different countries?
4. What differences, if any, in your ethical principles and morals do you believe you would have to adjust to in negotiating with other cultures (see Figure 8.7)?
5. What adjustments to your values and ethical decision-making style have you had to make in teams in your own culture, and with others from different cultures in your studies and/or work? Explain.
6. What is the difference between a gift and a bribe? How would you, as a representative of your company, respond to the offer of a questionable bribe from an international government or business professional? Explain.
7. Does globalization result in cultural and economic homogenization (alikeness) through a heightened emphasis on consumerism, or is this an exaggeration? Explain and defend your position.
8. Do local and global values change as a result of international integration? Why or why not? If so, in what ways? Offer a few examples.
9. Do you believe that globalization "promotes the conversion of national economies into environmentally and socially harmful export-oriented systems for business competition" that is not in the best interests of consumers? Why or why not? Defend your position.
10. Select two global companies mentioned in this chapter and locate their corporate web sites. Find their codes of conduct or ethics statements. Download these and evaluate whether or not they serve any practical purposes or help meet the companies' social responsibility goals and why.
11. Explain what the "dark side" of globalization means to you. Offer some examples. Offer an additional issue that could be considered a dark side of globalization. After doing so, offer a realistic solution that could either eliminate, change, or transform the dark side of your issue.
12. Do you believe Facebook, MySpace, and other such social-networking sites are, will, or can promote more commonly shared values of people across cultures–knowing that some countries have their own such web sites in their language? Explain.

13. Are you or have you thought about becoming a "social entrepreneur"? Do you believe this practice and movement can help make a difference in the world? Explain.
14. Explain the differences in perception and experience with regard to moral issues for (a) a host country viewing an MNE and (b) an MNE viewing a host country. Which perspective are you more inclined to support or sympathize with? Why?
15. In a paragraph or list, describe dominant cultural characteristics of yourself as could be seen from another country or regional perspective. Include some of your core values. Then proceed to the next question.

    Using your description from question 15, what difficulties or misunderstandings, based only on your answer, would you predict that you might encounter when negotiating an ethical dilemma with someone who had opposite cultural characteristics? Explain.

Exercises

1. Argue and defend your positions on the following statements:
   (a) The United States is already and will continue to lose its status as a central, pivotal global superpower, including its cultural and values influence, in the world in the next 10 to 20 years, if not sooner.
   (b) Censorship restrictions in other countries on such information technology as Google and other web sites are justifiable; the United States and other Western nations should not try to impose their values and norms on censoring practices.
   (c) A "global set of ethics" is impossible. Each culture and region of the world should have its own ethics as well as values and cultural differences.
   (d) To succeed, globalization must involve justice and fairness practices from First World countries toward Third World nations and peoples.
   (e) Although it is preferable that transnational and multinational companies act ethically, it is really not practical in every region of the world, including the United States.
   (f) MNEs cannot financially afford to follow the guidelines in Section 8.5; it would be too costly for them.
   (g) When two MNEs are both right on a controversial issue—for example, violation of patent or intellectual property rights—ethics should be avoided, and other, more concrete issues should be used to resolve the dispute.
   (h) Without transnational companies and MNEs doing business in poorer countries, peoples of those countries who are striving to survive would suffer even more.
2. Offer an example of and explain why one of your own values or an ethical standard you deeply believe in and follow might conflict with a different cultural or regional ethic in, for example, China, Russia, the Middle East, or the United States (if you are from a different culture). How flexible would you be,

or not be, in negotiating one of your core beliefs in another culture? What would be your constraints on being flexible and changing your value-based position? Explain.

3. Evaluate and argue different sides of this statement: "McDonaldization is not a 'bad' thing. Everyone has a choice of what and how much to buy and consume. People are lucky to have a low-cost food option like McDonald's."

Real-Time Ethical Dilemma

You (Jane) are a 29-year-old single woman who has an MBA and has been working in your current marketing position for a year. Your firm recently opened a new pilot branch in a somewhat remote Russian location. The CEO of your company believes there are real growth opportunities for your firm's products in that region and also wants visibility there. The company has decided to launch a small office there for visibility as well as to introduce the product. You are one of the most outgoing and talented marketing professionals in your firm. It is believed that you'll make a positive impression and represent the company well. There is a small community of American business professionals there who will assist you.

Country values there are very different from what you are accustomed to. You overhear a discussion between two of your male colleagues who were recently in that country completing arrangements for the office. One says, "Jane's going to have some interesting challenges with the men she has to do business with. . . . It's like the Wild West." The other answered, "Yeah, she's got some real surprises coming." Your research suggests that country laws and norms on issues you take for granted (like women's rights and sexual harassment) are not well defined.

You have a conflict over wanting to advance with your company but not wanting to take this assignment. You are aware that the CEO has his mind set. In fact, you've already had a discussion expressing your concerns and fears. He brushed your issues aside when he told you earlier, "Jane, try it. You need the international exposure and experience." The second time you approached him with your concerns, he blurted out, "Look, Jane. I understand your concerns, but this is important to me and our company. There are some people there who can help you. I know it's going to be a challenge. But after a couple of years, you'll thank me." You still don't feel right.

Questions

1. What do you do, and why?
2. If you do decide to go, what specific preparations should you make?
3. If you decide not to go, draft out the dialogue you would have with your CEO.

Real-Time Ethical Dilemma

You are attending a sexual-harassment training seminar for local managers in your company's branch office in a Middle Eastern, predominantely Muslim, country. You were flown over with the trainers to observe their techniques and become familiar with the training materials because you, as a new human resource staff member, would be expected to give this course. The course has been a success for managers in the United States. The same materials have been perfected and are being used in the United States. The instructors call on local Muslim managers (men and women) to role-play and openly share stories about sexual harassment that involved them or that they had heard about. Near the end of the half-day session, several of the host country employees uncharacteristically walk out. The trainers are dazed and become upset.

Questions

1. What do you think went wrong?
2. What would you do in this case if you were one of the trainers?
3. Read the epilogue following, then return and answer this question: Assume the trainers have been briefed on the research you just read. Who should do what, if anything, with the Muslim managers after this cultural mishap? Why?

Epilogue

"In 1993, a large U.S. computer-products company insisted on using exactly the same sexual-harassment exercises and lessons with Muslim managers halfway around the globe that they used with American employees in California. It did so in the name of 'ethical consistency.' The result was ludicrous. The managers were baffled by the instructors' presentation, and the instructors were oblivious of the intricate connections between Muslim religion and sexual manners.

The U.S. trainers needed to know that Muslim ethics are especially strict about male/female social interaction. By explaining sexual harassment in the same way to Muslims as to Westerners, the trainers offended the Muslim managers. To the Muslim managers, their remarks seemed odd and disrespectful. In turn, the underlying ethical message about avoiding coercion and sexual discrimination was lost. Clearly sexual discrimination does occur in Muslim countries. But helping to eliminate it there means respecting—and understanding Muslim differences."

Source

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Cases

Case 21

Google in China: Still "Doing No Evil"?

In 2010, "Google Inc. co-founder Sergey Brin pushed the Internet giant to take the risky step of abandoning its China-based search engine as that country's efforts to censor the Web and suppress dissidents smacked of the 'totalitarianism' of his youth in the Soviet Union." Although that decision took Google in a different direction, the company's 2006 decision to conduct business in China was based on an agreement that the company would offer a self-censored version ("Google.cn") of its search engine as required by the government in Beijing. The main issue critics had and have with Google's decision is that the company violated its own values and original philosophy, indicated in the statement "You Can Make Money without Doing Evil." For example, Beijing prohibits users from bringing up any results about "the Tiananmen Square protests of 1989, sites supporting the independence movements of Tibet and Taiwan or the Falun Gong movement and other information perceived to be harmful to the People's Republic of China."

The Chinese government's strict Internet censorship policy screens what users can access. A user of Google.cn who tries, for example, to access "the Falun Gong spiritual movement" is denied access and is directed to a string of condemnatory articles of that movement. A Google spokesperson said that its e-mail, chat room, and blogging services would also not be made available, since the Chinese government could demand users' personal information. A Google spokesperson did say that the company planned to notify users when access had been restricted on particular search terms.

Google's Response

Google offered an explanation of their position to operate in China on the Chinese version of Google News China on September 28, 2004. The following is an excerpt:

> "There has been controversy about our new Google News China edition, specifically regarding which news sources we include. For users inside the People's Republic of China, we have chosen not to include sources that are inaccessible from within that country. This was a difficult decision for Google, and we would like to share the factors we considered before taking this course of action. For Internet users in China, Google remains the only major search engine that does not censor any Web pages. However, it's clear that search results deemed to be sensitive for political or other reasons are inaccessible within China. For last week's launch of the Chinese-language edition of Google News, we had to decide whether sources that cannot be viewed in China should be included for Google News users inside the PRC. Naturally, we want to present as broad a range of news sources as possible. For every edition of Google

> News, in every language, we attempt to select news sources without regard to political viewpoint or ideology. For Internet users in China, we had to consider the fact that some sources are entirely blocked. Leaving aside the politics, that presents us with a serious user experience problem. Google News does not show news stories, but rather links to news stories. So links to stories published by blocked news sources would not work for users inside the PRC—if they clicked on a headline from a blocked source, they would get an error page."

A Google spokesperson stated in another interview that the company can play a more helpful role in China by being there than by boycotting the invitation, even with the concessions. "While removing search results is inconsistent with Google's mission, providing no information (or a heavily degraded user experience that amounts to no information) is more inconsistent with our mission," a statement said.

Business Incentives

Why do business in China? China is the world's largest online Internet market, when projected through the year 2008, according to the China Internet Network Information Center (CNNIC). The total number of users in China was estimated at 210 million at the end of 2007. The Nielsen/NetRatings estimated the U.S. Internet population at 216 million during that same period. Statistics from the CNNIC show that there are 107 million Internet users in China below age 25; that is almost half of the online population. "These users are ahead of the curve when it comes to social media and new technology take-up. About 33% of young Web users said they had updated their blogs within the previous six months, higher than the average of 23.5% across all users. Similarly, more than 30% said they had used mobile phones to surf the Internet, again higher than the national average."

Although Google was a late entrant to the China market (behind Yahoo, AOL, and Microsoft), it accounted for 26% of that country's Internet-search revenue in the fourth quarter of 2007, up from 17% in 2006, according to Beijing research firm Analysis International. Baidu.com's (China's online search leader) share of the market climbed from 58% to 60% during the same period.

Other Internet Companies Enter China

Google followed some of its competitors and related technology firms into China. Yahoo!, AOL, Microsoft, MySpace, and Skype also agreed with China's censorship requirements. Yahoo first purchased a $1 billion, 40% stake in Alibaba .com, which owned China's largest auction site. Following this transaction, eBay, Amazon, and InterActiveCorp—owner of online travel firm Expedia—purchased Chinese firms outright during 2004–2005. Google—before negotiating for direct access in China—acquired a small strategic stake in the online retailer Baidu .com (it has since sold that 5% stake). MySpace, owned by Rupert Murdoch's News Corp., used a strategy that Yahoo and eBay adopted—to operate as locally owned and managed businesses. MySpace is run by IDG, MySpace Inc., and China Broadband Capital Partners LP.

Google's competitiveness ranked first followed by Yahoo! for the sites that captured the majority of the search share in the region. Interestingly, "five of the top ten search properties are local country companies, including China's Baidu .com (16.7 percent) and Korea's NHN Corporation (5.3 percent), which owns search engine Naver.com. Chinese properties Alibaba.com Corporation, Tencent Inc., and Sohu.com Inc., which host Internet-search functionality although they are not strictly search engines, rounded out the list of key local players."

Controversies within the Great Wall

Google and its Western counterpart companies have faced controversies in the China relationship. For example:

- Yahoo was accused in 2005 of supplying data to China that was used as evidence to jail a Chinese journalist for 10 years;
- Microsoft agreed to censor content from its blog service, Windows Live Spaces, stating that providing Internet services is more helpful to the Chinese than not having a presence in that country;
- MySpace's Chinese version, which was launched in April of 2007, omitted and filtered certain discussion forum topics such as religion and politics.

Other topics such as the Dalai Lama and Taiwan independence were also blocked. Users on the web site were also able to report "misconduct" of other users for offenses including "endangering national security, leaking state secrets, subverting the government, undermining national unity, spreading rumors or disturbing the social order." Guo Quan's quarrel with Google is more recent: "Guo Quan, an expert on classical Chinese literature and the 1937 Nanjing massacre of Chinese civilians by Japanese troops . . . issued [in March 2008] an open letter pledging to bring a lawsuit against Google after he discovered that his name had been excised in searches of its Google.cn portal in China." Quan, in the open letter stated, "To make money, Google has become a servile Pekinese dog wagging its tail at the heels of the Chinese communists." Again, just beneath the impressive business competitiveness and strategic prowess of the Western search companies in China lies moral issues that will not be silenced.

Google in China: Face of the Future? Or Derailed from Its Values?

At a University of California, Berkeley gathering in February 2006, just after Google signed on with China, students chanted "Shame on Google" and "Google, don't be evil," before the then Google China president Kai-Fu Lee spoke. "Students for a Free Tibet," a group that was critical of Google's action in China, held signs at the meeting, one stated "Kaifu Leevil." Alma David, a member of this group and a University of San Francisco law school student, said, "We hope to get the message to Kai-Fu Lee that we won't stand for censorship. We see a company selling out its values for a profit. Its 'don't be evil' just seems like a bad joke." Orville Schell, dean of the journalism school of the University of California at Berkeley said, "We are now witnessing the price that companies are willing to pay in

order to buy in to China. The business side of the world we're meeting here simply feels that China cannot be ignored."

Cheng Siwei, vice chairman of the National People's Congress of China, said in a 2006 interview in response to Google's agreement with China that democracy was his country's final goal. "But we must go step by step. We were a backwater country. To speak frankly, there are still anti-Chinese groups spreading rumors about our policies in order to raise suspicion among our people. We need to have some control." Victor Chu of First Eastern Investment Group commented that "foreign criticism had failed to recognize that change enters China slowly. The trade-off of Google's decision to set up even a censored search engine can help that process along. The commentaries are wrong that Google's entry into China is a sad day for free expression. We should be glad that Google has started a process that is good for free expression. Ideally, of course, China would open up to Google and all foreign media entirely. But that will not happen overnight, and meanwhile, Google has positioned itself very well indeed as a business."

Frida Ghitis, a writer on world affairs, expressed another view in the *Boston Globe*:

> Now Google has become a company like all others, one with an eye on the bottom line before anything else. The company has decided to help China's censors even as it fights a request for records from the U.S. Justice Department's investigation of online child pornography. Skeptics had claimed Google was resisting the request in order to protect its technology, rather than to protect users' privacy. That explanation now sounds more plausible than ever.

We've long known about China's disdain for individual freedoms. But Google, we hardly knew you. It's definitely time to rethink that Gmail account and demand some safeguards from a potentially dangerous company. Perhaps here, too, we will need to heed the Tibetan cybercafé warning, "Do not use Internet for any political or unintelligent purposes."

Google's Push and Pull

Google has reluctantly conceded defeat in its latest effort to combat online censorship in China, after a year of behind-the-scenes brinkmanship over sensitive search terms banned by authorities. In May 2012, the search company has quietly dropped a warning message shown to Chinese users when they search for politically sensitive phrases, after Beijing found new ways to cut them off from the web. Within 24 hours of the feature being launched, it was disabled by Chinese authorities. Days later, in June 2012, Google modified how the notification would appear for users—but that too resulted in another block. In November 2012, Google's English-language and Chinese-language services were blocked for 24 hours as tensions stepped up. Google resolved to drop the notification features in early December after users continued to report problems for certain searches. Google continues to battle the Chinese government on this issue.

Questions for Discussion

1. What is at issue from your reading of this case?
2. Do you agree or disagree with Google in this case? Explain.
3. What is your reaction or response now to this statement made by a Google spokesperson in 2006? "While removing search results is inconsistent with Google's mission, providing no information (or a heavily degraded user experience that amounts to no information) is more inconsistent with our mission." Is this still Google's position?
4. (a) Defend Google's argument(s) in accepting to do business in China. (b) Defend the critics who argue that Google betrayed its values when entering China.
5. (a) What ethical principle(s) did Google use (and is now using) to do business in China with its censorship policy? Has anything changed on Google's part? Explain. (b) What ethical principle(s) are Google's critics in the case using in not accepting Google's presence in China?
6. What effects will Google's recent lack of censorship have on Chinese relations with the United States?

A Note on Falun Gong

Falun Gong or Falun Dafa is a spiritual practice founded in China in 1992; the books based on this practice are translated into 40 languages. The practice relates to moral standards, character, salvation, and virtue. One estimate of followers of this practice approximates 70 million. China's government considers Falun Gong an organized political group that opposes the Communist Party of China and the central government. The group was banned in mainland China in 1999. Since that time, a U.S. State Department report and UN reporter concur that almost 70% of all torture incidents involve those who practice Falun Gong. This description is based on the following sources:

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Case 22

Sweatshops: Not Only a Global Issue

The Idea

Imagine that every day you go to work you are exposed to toxic chemicals without having any protective clothing or safety training, and that the workplace has poor ventilation and poor fire safety. Suppose that you are subject to physical and verbal abuse at the hands of your employer and that there is a lack of drinking water in the workplace. Suppose further that you are paid only a couple of dollars per day and forced to work excessive overtime hours. Would these be satisfactory working conditions—for anyone, anywhere in the world? Conditions such as these are found in businesses commonly known as sweatshops. "Migrants are constantly in a state of danger . . . they are in a constant state of stress. But they are needed and are beneficial to those that keep on exploiting them," said Svetlana Gannushkina of the human rights group Assistance for Citizens.

The Move

Sweatshops exist throughout the world and in a variety of manufacturing industries, including apparel, shoes, toys, and electronics, among others. They have become most notoriously famous within the footwear and apparel (or garment) industries. In these two industries, easy portability of work and technology from one region to another, or one country to another, has facilitated the ongoing presence of and reliance on sweatshop factories. For instance, from a historical perspective, apparel manufacturing has been a very mobile industry. It has migrated from Britain to New England in the United States, to the Southeastern United States, to Mexico and Asia, with companies constantly pursuing less-expensive workers, a practice often referred to as "the race to the bottom." In this race, clothing wholesalers and retailers have developed a manufacturing supply chain of a large number of contractors and an even larger number of subcontractors, all with the aim of securing the absolutely lowest cost anywhere in the world. Each move in the race to the bottom has been more fleeting than the preceding one, with an excruciating toll being exacted from the workers at the lowest rungs of the "economic food chain" for the predatory benefit of others higher up and at the top.

Of course, this race to the bottom has not been confined to the footwear and apparel businesses. It is occurring in the production of computer motherboards, printers, laptops, and other electronics equipment. It can be found in any type of business that supplies products to large retailers—like Wal-Mart and Target—that operate on the basis of a low-price strategy. "These giants increasingly control the pricing power in overseas manufacturing that in turn dictates how much money factories can spend on improving labor conditions." Moreover, "Anti-sweatshop efforts are fatally undermined by the schizophrenia of the transnational 'brands' themselves. The brands' sourcing department pays ever-diminishing prices for the products (with ever-shortening delivery times) while the same brand's CSR [corporate social responsibility] department requires compliance with the mini-

mum wage and hours of work limits in the brand's code and local laws, often combined with other CSR initiatives to be paid for entirely by the contractors. If the contractor doesn't like this deal, then the brand will find someone else who will meet the order as offered."

The Problem

A Georgetown study showed that people were more likely, for example, to endorse the use of questionable labor practices involved in a Caribbean vacation for themselves, but tend to oppose that use if the vacation in question is for their friends.

"This phenomenon, known as moral hypocrisy, is used by consumers in situations to benefit themselves but not others," study author Neeru Paharia explains. "They also made economic development justifications, such as convincing themselves that sweatshops are the only realistic source of income for workers in poorer countries, without which they wouldn't develop, that the labor offers products not otherwise affordable to low-income people and it's OK because 'companies must remain competitive.' "

"A great sale or exclusive offer can increase the desirability and value of a product, which can further justify the labor practices used to create the product," Paharia says. "The strength of a brand and consumer loyalty may also influence reasoning—causing consumers to view companies such as Nike and Apple as subsidiaries that are not directly involved with the labor conditions."

The Fight

Unfortunately, most companies that are "benefiting from sweatshop labor around the world are doing nothing about it." According to the Investor Responsibility Research Center, just 12% of S&P 500 companies have formal requirements that their suppliers address labor issues and only 4% have requirements that address all the issues—including the freedom to organize bans on child labor, forced labor, and discrimination—considered to be important by the International Labor Organization. "The latest corporate social responsibility (CSR) reports from companies like clothier Gap Inc. and toy-maker Mattel and multistakeholder organizations like the Fair Labor Association and Workers Rights Consortium all document that sweatshop conditions in every country (including the U.S.) are alive and well."

In April 2013, a Bangladeshi factory building collapsed killing more than 1,100 employees. Following this horrific sweatshop-related disaster, opinions from every side of the aisle have been reigning in over how to stop these practices. Yet it is hard to get away from the fact that without the sweatshop the employees would have no job whatsoever.

Given that sweatshop conditions exist around the world, what can be done to counter these assaults upon human dignity and human rights that affect the most vulnerable people in the "economic food chain"? Not surprisingly, in the context of prevailing macroeconomic conditions and pent-up demand for low-cost production, the prospect of black market sweatshops becomes all too real. The

problem could be addressed at the other end of the supply chain. Western retailers should be required to display details of their full supply chain to consumers and invest in monitoring conditions at all stages. The "fair trade" concept could then be applied to all types of industries, allowing consumers the choice of paying a small premium on products produced in acceptable working conditions.

During the past several years a number of avenues of activism against sweatshops have emerged. For example, in the United States, student-led anti-sweatshop demonstrations and protests pressured some 200 colleges and universities into adopting "no-sweat" purchasing policies—especially for clothing emblazoned with the schools' logos. Ten universities in Canada also have "no-sweat" buying policies, as do several U.S. and Canadian cities. The Worker Rights Consortium (WRC) campaigns against sweatshops and helps to police factory compliance with "no-sweat" codes of business conduct. The WRC "does complaint-based and spot monitoring of plants that supply goods to its over 100 member universities."

In 2003, the Fair Labor Association (FLA), whose members include companies such as Adidas-Salomon, Eddie Bauer, Inc., Levi Strauss & Co., Liz Claiborne Inc., Nike, Inc., the Phillips-Van Heusen Corporation, and Reebok International Ltd., as well as about 175 colleges and universities, began publicizing audits of factories regarding possible sweatshop conditions, including labor and human rights violations. These publicized audits put "pressure on Wal-Mart, Disney, Gap, and every other company that does labor monitoring, to release their audits, too." In May 2004, Gap, Inc. issued its first social responsibility report in which it acknowledged that "many of the overseas workers making the retailer's clothes are mistreated and [the company] vowed to improve shoddy factory conditions by cracking down on unrepentant manufacturers." Gap uncovered "thousands of violations at 3,009 factories scattered across roughly 50 countries," including unacceptably low pay, psychological coercion and/or verbal abuse, lack of compliance with local laws, workweeks in excess of 60 hours, poor ventilation, and machinery lacking operational safety devices. Gap CEO Paul Presser says, "We feel strongly that commerce and social responsibility don't have to be at odds."

These are some of the more notable efforts that have been undertaken to combat sweatshop conditions around the world. They have met with varying degrees of success. Ultimately, however, true success only will be found in putting the brakes on the "race to the bottom," and in establishing an acceptable minimum level of conditions and compensation for workers on the lowest rungs of the "economic food chain"—acceptable minimums that will ensure them a living wage, protect their rights, and respect their dignity as human beings.

Currently, three major groups oversee factory inspections to monitor sweatshop conditions. These are Social Accountability International (SAI), with members including Toys "R" Us and Otto Versand, the German direct-mail giant; the FLA, which was established by footwear and apparel makers such as Nike, Reebok International, and Liz Claiborne; and the Ethical Trading Initiative (ETI), a London-based organization composed of European unions, companies, and nonprofits. All three groups have codes of conduct that specify standards and also

oversee factory monitoring targeted toward enforcing their codes and remedying violations of the standards.

Due to considerable variation in the methodologies used by SAI, FLA, and ETI, many companies have engaged in some form of self-monitoring. For instance, "Wal-Mart says it inspects thousands of supplier factories each year in dozens of countries. But since no outside body such as SAI or the FLA is involved and Wal-Mart won't release its audits or even its factories' names, the public is left to take the company's word for it." However, the perceived confusion among the methodologies of SAI, FLA, and ETI appears to be on the verge of changing as a consequence of an ambitious 30-month experiment called the Initiative on Corporate Accountability and Workers' Rights, which is being sponsored by six anti-sweatshop activist groups and eight global apparel makers. This initiative seeks "to devise a single set of labor standards with a common factory-inspection system that will 'replace today's overlapping hodgepodge of approaches with something that's easier and cheaper to use—and that might gain traction with more companies.' If it works, the 30-month experiment would create the first commonly accepted global labor standards—and a way to live up to them."

"This 30-month experiment is a great first step in bringing order to the piecemeal manner in which even the biggest companies set and monitor workplace conditions across the developing world. But a much broader solution is required to make real progress against sweatshop conditions. There are currently only about 100 large, mostly Western companies actively involved in the anti-sweatshop movement. Their efforts over the past decade are laudable but ultimately insufficient because thousands of other manufacturers don't participate. Building consensus around basic universal standards for particular industries, say apparel or consumer electronics, is crucial. Otherwise, why should one manufacturer incur the cost of upgrading and continually monitoring its workplace standards if it has to compete with factories without the same obligations?"

Questions for Discussion

1. Why are sweatshops so common around the world?
2. Why are sweatshops viewed with disgust and abhorrence? Does a sweatshop accomplish anything positive?
3. What is a reasonable objective (or set of objectives) for addressing sweatshop conditions throughout the world? Explain your answer.
4. What is your assessment of the potential of the Initiative on Corporate Accountability and Workers' Rights for making significant progress in alleviating sweatshops around the globe?
5. Do you think "moral hypocrisy" has any effect in the fight to improve working conditions in sweatshops? Explain your reasoning.

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Case 23

The U.S. Industrial Food System

"The way we eat has changed more in the last 50 years than in the previous 10,000. But the image that's used to sell the food, it is still the imagery of agrarian America." In the grocery store we see labels picturing pastures and names of farms on the labels; in reality, however, it is a handful of corporations bringing our food to market, not farmers. Corporations use farm-fresh images to create a specific brand image. The biggest names in the industry are: ADM, Cargill, ConAgra, IBP, Monsanto, Swift, and Tyson. These multinational corporations control our food from seed to supermarket and have different methods of communicating information about that food to consumers. In the 1970s, the top-five beef packers controlled 25% of the market. Today, the top four companies control more than 80% of the market. Meat-packers, slaughterhouses, seed manufacturers, and food processors operate like monopolies in their control of the U.S. food industry.

The corporations running the food supply chain in the United States are constantly enhancing production to create larger quantities of food at lower costs. More efficient production processes allow for the distribution of food products to more parts of the world. Yet, the process is not without concern. Food industry jobs are often endangering to employees. Animals are raised and treated in controversial conditions, and many employees find themselves responsible for treating meat with chemicals like ammonia, which creates health issues like diabetes, obesity, and cancer. This, in turn, increases demand for medical professionals and the need for prescription drugs. The effect on stakeholders may even go as far as increasing American reliance on fossil fuels, aggravating the deportation of illegal farm workers whose labor is essential to this food industry, and further increasing children's addiction to sugar and sweetening substitutes. Where's the efficiency in that?

A Brief History of Food since 1800

In the early 1800s, the independent farmer was considered the bedrock of American democracy. It wasn't until the 1950s that the McDonald brothers introduced a factory assembly line to a commercial kitchen for the first time. The assembly line process taught workers a single task; significantly increased efficiency; and, in essence, created the fast food industry. Today, "McDonald's is the nation's largest purchaser of beef, pork, and potatoes—and the second largest purchaser of chicken." This strong purchasing power gives fast-food franchise giants, like McDonald's and Burger King, influence over food supply. This has resulted in diminished need for independent farmers; in fact, prison inmates in the United States now outnumber farmers. Without a network of independent farmers, once the backbone of this country, our food supply must now be controlled by major corporations. Throughout history we have never seen food companies this large and with this much power.

The processing/refining of our foods has also changed significantly in the last century. Americans generally no longer eat "whole" foods like vegetables,

fruits, and whole grains; instead, they rely primarily on processed foods. Processing makes more money for corporations, but at what cost to the consumer? "It is a fact that the chronic diseases that now kill most Americans can be traced directly to the industrialization of food: the use of chemicals to raise plants and animals in huge monocultures; the superabundance of cheap calories of sugar and fat produced by modern agriculture; and the narrowing of the biological diversity of the human diet to a tiny handful of staple crops, notably wheat, corn, and soy. These changes have given us the Western diet that we take for granted: lots of processed foods and meat, lots of added fat and sugar, lots of everything–except vegetables, fruits, and whole grains."

The Industrial Food Supply Chain

Unethical activity takes place at all steps of the industrial food supply chain: the animals; the growers of our food, the workers in their factories, the influence extended on our legal system, the planet Earth, the health care system, and ultimately the consumer.

The Treatment of Animals

Cows, natural-born grazers of grasses, are now raised on feedlots called Concentrated Animal Feedlot Operations (CAFO), created after World War II to make the production of meat more efficient. On CAFOs, cattle's diet consists mainly of corn, which fattens them quickly, but also animal byproducts including cow's blood (a substitute to mother's milk when cows are taken from mothers at less than 24 hours old), out-of-date domestic pet food, antibiotics, and even poultry litter. Until the Food and Drug Administration's (FDA) ban in 1997 after discovering it led to mad cow disease, cows were even fed broken-down cow parts. Cows are housed in small pens, never allowed to graze in pastures, and stand in pools of their own excrement. What was formerly a well-functioning system—cattle grazing on the waste of crops fertilizing the soil, making it rich to grow more crops—is now a system resulting in two new inefficiencies: a fertility problem on the farm, requiring chemical fertilizers to remedy; and a pollution problem in the feedlot, which is often not remedied at all.

A fatal consequence of cattle's new diet is the creation of *E. coli* 015:H7 in the cow's stomach, which, in turn, lives in the meat purchased and consumed by consumers. The acid in our stomachs cannot destroy *E. coli* 015:H7. The virus can and has killed humans, including 2-year-old Kevin Kowalcyk of Colorado, an otherwise healthy boy. Without the human intervention of feeding corn to cattle, this virus would never even exist. Studies have shown that if cattle were removed from feedlots and allowed to graze on grass for just a few days before slaughter, 80% of *E. coli* would be eliminated. Yet the cattle industry and the United States Department of Agriculture (USDA) consider that an impractical solution to the problem.

The 2008 documentary *Food, Inc.* also reveals the disturbing treatment of chickens in the food industry. Like cattle, chickens are fed corn and antibiotics to fatten them more quickly and efficiently. The time to maturity has been reduced

by more than 30% since the 1950s. Chickens are fattened so quickly that their bones, muscles, and internal organs are not strong enough to support them. The disturbing footage in *Food, Inc.* shows several birds who can take only a few steps before collapsing beneath the weight of their supersized corn-fed breasts. White meat is of the highest demand in the fast-food industry. The chickens live in tight quarters, stepping over each other and in each other's waste. The animals never see any sunlight, living in a large tunnel-like chicken house required by large corporations like Purdue and Tyson.

The Treatment of Growers and Factory Workers

Chicken growers typically begin the process by building one or more poultry houses and signing a contract with one of the major chicken retailers in the country (i.e., Tyson or Purdue). The building of two poultry houses can land the grower with a mortgage of about $500,000; whereas, the average yearly salary of a grower was only $18,000 in 2009. This grower then must conform to all regulations set by the corporation, including costly equipment purchases and upgrades to the poultry houses. Failure to do so results in a loss of contract. One grower interviewed in *Food, Inc.* discussed the stench and illness inside the poultry house. She developed an allergy to all antibiotics as a result of growing chickens. Chickens spend their entire lives as corporate property. Why don't corporations grow their own chickens? They have found that outsourcing to chicken growers produces the same results at a much lower cost. Once the animals are fully grown, catchers are sent in to collect them. The chicken catchers hired by corporations were formerly poor Americans but are now primarily undocumented Latino workers.

Slaughterhouse workers are said to have one of the most dangerous jobs in the country. Both *Food, Inc.* and Eric Schlosser's *Fast Food Nation* discuss the horrific conditions, life-threatening injuries and illnesses, lack of unions, low number of inspections, minimum-wage salaries and nonexistent benefits faced by employees working in meat-processing plants. These conditions are true of employees who either clean the facilities or handle the meat. Most often, it is illegal immigrants performing the most treacherous and lowest-paying jobs.

Poor conditions are also found in the growing process of other foods of popular demand. The profession of potato farmers, for example, has drastically changed. Potatoes, which once thrived on farms in Maine, are now mass-produced in Idaho. It is estimated that about 2 cents of every $1.50 order of fast-food fries makes it back to the farmer. Like the chicken grower, the average potato farmer is more than $500,000 in debt before even earning a penny.

The fast-food service industry itself is also a source of worker exploitation. Fast-food chains rely heavily on unskilled, low-paid workers. "The roughly 3.5 million fast food workers are by far the largest group of minimum wage earners in the United States."

The grower, farmer, factory or service worker puts himself or herself at risk both financially and physically.

The Legal System

Government subsidies make corn a natural choice for animal feed. Corn is now the cheapest food source available and fattens the animals most quickly. This is a result of farm bills passed with pressure from Congressional lobbyists representing the big companies like Cargill, Smithfield, Tyson, and others. The North American Free Trade Agreement (NAFTA) resulted in cheap American corn in Mexico, putting approximately 1.5 million Mexican corn farmers out of business. Large meat processors like IBP actively recruited in Mexico for cheap labor in their slaughterhouses. *Food, Inc.* shows footage of the government taking illegal immigrant workers into custody at their homes, but never at the slaughterhouses. The film suggests that Smithfield meat processor has an arrangement with the government to provide the whereabouts of 15 illegal aliens each day at their homes in exchange for the government's avoidance of the corporation's factories.

In 1977, Senator McGovern chaired the Senate Select Committee on Nutrition and Human Needs to probe the link between diet and the increase in chronic diseases like heart disease, cancer, obesity, and diabetes. The committee found that during war time, when U.S. consumption of meat and dairy was down, rates of heart disease similarly dropped. They also noted that in countries where diets are based mostly on plants, rates of chronic diseases were "strikingly low." The committee went on to publish dietary guidelines suggesting that Americans cut back on red meat and dairy products. The threatened red meat and dairy industries forced the committee to change its recommendation from "reduce consumption of meat" to "choose meats, poultry and fish that will reduce saturated fat intake." In the next election, three-term senator McGovern was ousted, demonstrating the potential repercussions for politicians who take on the food industry.

In the 1980s, a U.S. law was passed allowing companies to put a patent on life. As a result, the corporation Monsanto owns a genetically modified organism (GMO), a type of soybean, grown in the United States. These specific soybeans were created to withstand the spraying of pesticide on crops (another Monsanto product). The GMO soybean withstands pesticides and herbicides better than any other. Farmers must now purchase fresh seed from Monsanto every year or take the serious and expensive risk of being sued by Monsanto and put out of business. These seeds are proven to grow more efficiently, but no one yet knows the health consequences humans face from eating GMOs. Interestingly, *Forbes* magazine named Monsanto the "Company of the Year" in 2010. The article explained Monsanto's plan to reach other nations, such as China, who will need GMO grains to raise enough steak to feed the masses and bring the Western diet to Asia.

"Every day in the United States, roughly 200,000 people are sickened by food borne disease, 900 are hospitalized and fourteen die." After the 2 year old mentioned above tragically died as a result of eating beef containing *E. coli* 015:H7, his mother became an advocate fighting for higher safety standards in our food industry. For several years she has been working to have a bill passed into law: the Meat and Poultry Pathogen Reduction and Enforcement Act of

2003, also known as "Kevin's Law." This law would give the USDA the power to close down plants that produce contaminated meat. This bill is still not a law.

Food, Inc. shows viewers that many politicians and regulatory committee members have ties to large food industry corporations. For several years the chief of staff to the USDA was a former chief lobbyist to the beef industry, and the head of the FDA was the former executive vice president of the National Food Processors Association. In January 2010, the Supreme Court ruled to "overturn a 20-year-old Supreme Court ruling that barred corporations from spending freely to support or oppose candidates." Corporations are now able to pour as much money as they want into advertisements for or against a particular candidate. The food industry giants are among the wealthiest corporations in the world.

The Planet

The use of fertilizers on crops inhibits the crops' ability to obtain nutrients from the soil, resulting in a less nutritious fruit or vegetable. Additionally, growing only one crop repeatedly, as opposed to varying crops, further depletes the soil of nutrients. We are left with a downward spiral in the nutritional content of our fruits and vegetables. When the vitamin levels found in an apple from 1940 were compared to one grown today, only about one-third of the nutrients were present in today's apple. In addition to the depletion of nutrients in produce, the relatively new year-round need for out-of-season plants, particularly citrus, around the world requires the use of additional fertilizers, irrigation systems, and fossil fuels to plant, harvest, and transport.

The Fallout of the American Diet

Corn, wheat, and soybeans are very highly subsidized commodities in the United States that can be found in nearly every product in the supermarket. High fructose corn syrup, for example, is very common. This translates to a large increase in the sugar and empty calories found in American diets. Government subsidies make bad calories cheaper for consumption. Obesity, cancer, and diabetes are on the rise in every country that adopts the Western, or American, diet of processed and fast food.

As Senator McGovern's committee discovered in the 1970s, evidence points to the correlation of chronic diseases and industrialization of food in America. Farms today can "produce more calories per acre, but each of those calories may supply less nutrition than it formerly did. Nutritionists have known for years that a diet high in whole grains reduces one's risk for diabetes, heart disease and cancer," yet the industry makes more money off refined grains that can be stored and manufactured into a wider variety of packaged foods for purchase. This creates a greater demand on the U.S. health care system and drug industry.

Big Organics

As an alternative to conventional food products, organic meat and produce offer several improvements. Companies like Stonyfield Farms are growing over 20%

annually. Organics is the fastest-growing segment in the food industry. They are not as sustainable as independent farmers, but big organic corporations are improving the industry by using fewer pesticides and working to educate consumers.

Food Industry Corporations

These giant conglomerates make outlandish profits, billions more than their nearest competitors. They run their factories in hiding. None of the top corporations would agree to be interviewed for either of Michael Pollan's books (*In Defense of Food* and *The Omnivore's Dilemma*) or the documentary *Food, Inc.*

Ethical Implications

The stakeholder victims of the U.S. food industry are many: consumers, growers, farmers, factory workers, and service industry workers. Additional stakeholders include the shareholders of the food companies, professionals in the medical industry, health insurance industry, oil industry, transportation, government, and even foreign nations who are adopting the Western diet.

Over the last century the marketplace set a demand for larger quantities of cheaper food. Individuals were suffering from malnutrition, and during the Great Depression people could not afford to eat. The issue was how to make farming more efficient and increase the availability of products. However, in the attempt to make things more efficient, new and larger problems have resulted, changing the issue to one of a food and health crisis.

Stakeholders include the owners, customers, employees, suppliers, competitors, government, unions, customer advocate groups, and illegal immigrants. At first glance, it seems that these stakeholders are working in the best interests of many of the consumers. These stakeholders provide customers with accessible food products, they employee thousands in the United States, and they form relationships with countless suppliers. Upon closer inspection, however, the products created by the food industry that are readily available to customers are, in fact, leading to the increase in chronic diseases and rising health care costs. Employees are working in unsafe and often illegal situations with few or no benefits. Suppliers and farmers are being exploited. Many of these groups do not understand that they are victims. The government appears to be in a collaborative relationship with the industry. Politicians receive money from industry giants. Times are finally beginning to change with the new organic movement, however. Consumers are more educated about what the food system is doing to the health of their families. Stores like Whole Foods are catering to the highly educated consumer. Even Wal-Mart has begun selling organic foods, as it recognizes the shift in consumer demands.

Still, the U.S. food industry is in a crisis. Every time a child dies or an adult becomes sick due to *E. coli* in their food, the consumers, executives, and government should be outraged. Why hasn't Kevin's Law passed? Each year when health care costs rise, rates of cancer and heart disease skyrocket, and nutrients in foods are diminished, alarm bells should be sounding.

Conclusion

Consumers are becoming more educated and the food industry is slowly shifting to provide more options. Wal-Mart, for example, has adopted organic products. Farmers markets are seeing a resurgence as consumers demand healthier, greener options. As *Food, Inc.* pointed out, we don't buy the cheapest car, so why buy the cheapest food? Quality does matter. As consumers educate themselves and make demands for less processed foods, the industry will have to respond to changing demands.

Questions for Discussion

1. What are the most significant issues in this case and are these really that important to you?
2. Who are a few of the major stakeholders and their stakes in this case?
3. Are the issues in this case national or global in nature? Explain.
4. Who is responsible and why for problems presented and argued in this case?
5. Are there any, and if so please identify, positive steps being taken to rectify the problems this case presents?

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