

Chapter 3:

Ethics and Social Responsibility

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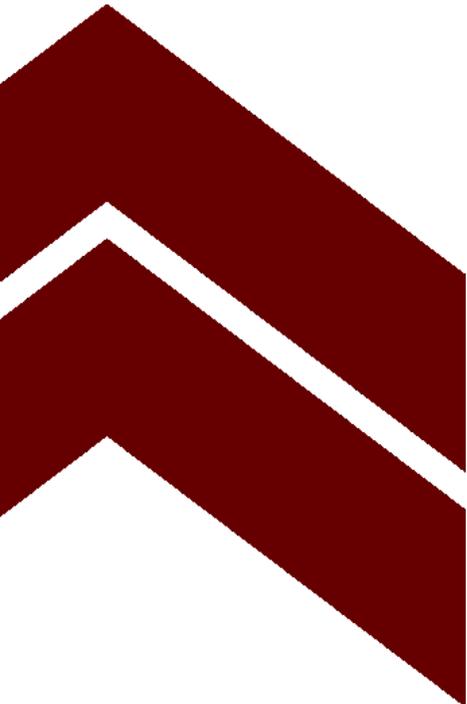
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Chapter 3

Ethics and Social Responsibility

Learning Objectives

- 1) Define business ethics and explain what it means to act ethically in business.
- 2) Explain why we study business ethics.
- 3) Identify ethical issues that you might face in business, such as insider trading, conflicts of interest, and bribery, and explain rationalizations for unethical behavior.
- 4) Identify steps you can take to maintain your honesty and integrity in a business environment.
- 5) Define corporate social responsibility and explain how organizations are responsible to their stakeholders, including owners, employees, customers, and the community.
- 6) Discuss how you can identify an ethical organization, and how organizations can prevent behavior like sexual harassment.
- 7) Learn how to avoid an ethical lapse, and why you should not rationalize when making decisions.

Introduction

“Mommy, Why Do You Have to Go to Jail?”

The one question Betty Vinson would have preferred to avoid is “Mommy, why do you have to go to jail?”¹ Vinson graduated with an accounting degree from Mississippi State and married her college sweetheart. After a series of jobs at small banks, she landed a mid-level accounting job at WorldCom, at the time still a small long-distance provider. Sparked by the telecom boom, however, WorldCom soon became a darling of Wall Street, and its stock price soared. Now working for a wildly successful company, Vinson rounded out her life by reading legal thrillers and watching her daughter play soccer.

Her moment of truth came in mid-2000, when company executives learned that profits had plummeted. They asked Vinson to make some accounting adjustments to boost income by \$828 million. Vinson knew that the scheme was unethical (at the very least) but she gave in and made the adjustments. Almost immediately, she felt guilty and told her boss that she was quitting. When news of her decision came to the attention of CEO Bernard Ebbers and CFO Scott Sullivan, they hastened to assure Vinson that she’d never be asked to cook any more books. Sullivan explained it this way: “We have planes in the air. Let’s get the planes landed. Once they’ve landed, if you still want to leave, then leave. But not while the planes are in the air.”² Besides, she’d done nothing illegal, and if anyone asked, he’d take full responsibility. So Vinson decided to stay. After all, Sullivan was one of the top CFOs in the country; at age thirty-seven, he was already making \$19 million a year.³ Who was she to question his judgment?⁴

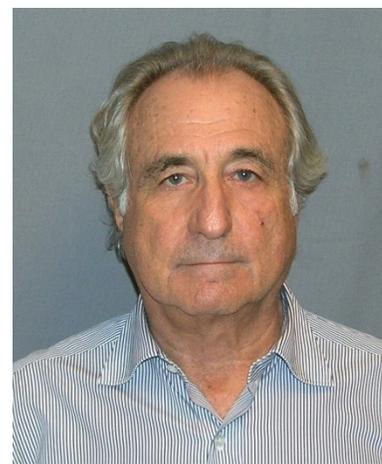
Six months later, Ebbers and Sullivan needed another adjustment—this time for \$771 million. This scheme was even more unethical than the first: it entailed forging dates to hide the adjustment. Pretty soon, Vinson was making adjustments on a quarterly basis—first for \$560 million, then for \$743 million, and yet again for \$941 million. Eventually, Vinson had juggled almost \$4 billion, and before long, the stress started to get to her: she had trouble sleeping, lost weight, and withdrew from people at work. She decided to hang on when she got a promotion and a \$30,000 raise.

By spring 2002, however, it was obvious that adjusting the books was business as usual at WorldCom. Vinson finally decided that it was time to move on, but, unfortunately, an internal auditor had already put two and two together and blown the whistle. The Securities and Exchange Commission charged WorldCom with fraud amounting to \$11 billion—the largest in U.S. history. Seeing herself as a valuable witness, Vinson was eager to tell what she knew. The government, however, regarded her as more than a mere witness. When she was named a co-conspirator, she agreed to cooperate fully and pleaded guilty to criminal conspiracy and securities fraud. But she won't be the only one doing time: Scott Sullivan will be in jail for five years, and Bernie Ebbers will be locked up for twenty-five years. Both maintain that they are innocent.⁵

So where did Betty Vinson, mild-mannered midlevel executive and mother, go wrong? How did she manage to get involved in a scheme that not only bilked investors out of billions but also cost seventeen thousand people their jobs?⁶ Ultimately, of course, we can only guess. Maybe she couldn't say no to her bosses; perhaps she believed that they'd take full responsibility for her accounting "adjustments." Possibly she was afraid of losing her job or didn't fully understand the ramifications of what she was doing. What we do know is that she disgraced herself and went to jail.⁷

The WorldCom situation is not an isolated incident. Perhaps you have heard of Bernie Madoff, founder of Bernard L. Madoff Investment Securities and former chairman of the NASDAQ stock exchange.⁸ Madoff is alleged to have run a giant Ponzi scheme⁹ that cheated investors of up to \$65 billion. His wrongdoings won him a spot at the top of Time Magazine's Top 10 Crooked CEOs. According to the SEC charges, Madoff convinced investors to give him large sums of money. In return, he gave them an impressive 8 percent to 12 percent return a year. But Madoff never really invested their money. Instead, he kept it for himself. He got funds to pay the first investors their return (or their money back if they asked for it) by bringing in new investors. Everything was going smoothly until the fall of 2008, when the stock market plummeted and many of his investors asked for their money. As he no longer had it, the game was over and he had to admit that the

Figure 3.1: Bernie Madoff's mug shot



whole thing was just one big lie. Thousands of investors, including many of his wealthy friends, not-so-rich retirees who trusted him with their life savings, and charitable foundations, were financially ruined. Those harmed by Madoff either directly or indirectly were likely pleased when he was sentenced to jail for one-hundred and fifty years.

What is Business Ethics?

The Idea of Business Ethics

It's in the best interest of a company to operate ethically. Trustworthy companies are better at attracting and keeping customers, talented employees, and capital. Those tainted by questionable ethics suffer from dwindling customer bases, employee turnover, and investor mistrust.

Let's begin this section by addressing this question: What can individuals, organizations, and government agencies do to foster an environment of ethical behavior in business? First, of course, we need to define the term.

What Is Ethics?

You probably already know what it means to be **ethical**: to know right from wrong and to know when you're practicing one instead of the other. We can say that **business ethics** is the application of ethical behavior in a business context. Acting ethically in business means more than simply obeying applicable laws and regulations: It also means being honest, doing no harm to others, competing fairly, and declining to put your own interests above those of your company, its owners, and its workers. If you're in business you obviously need a strong sense of what's right and wrong. You need the personal conviction to do what's right, even if it means doing something that's difficult or personally disadvantageous.

Why Study Ethics?

Ideally, prison terms, heavy fines, and civil suits would discourage corporate misconduct, but, unfortunately, many experts suspect that this assumption is a bit optimistic. Whatever the condition of the ethical environment in the near future, one thing seems clear:

the next generation entering business—which includes most of you—will find a world much different than the one that waited for the previous generation. Recent history tells us in no uncertain terms that today’s business students, many of whom are tomorrow’s business leaders, need a much sharper understanding of the difference between what is and isn’t ethically acceptable. As a business student, one of your key tasks is learning how to recognize and deal with the ethical challenges that will confront you. Asked what he looked for in a new hire, Warren Buffet, the world’s most successful investor, replied: “I look for three things. The first is personal integrity, the second is intelligence, and the third is a high energy level.” He paused and then added: “But if you don’t have the first, the second two don’t matter.”¹⁰

Identifying Ethical Issues and Dilemmas

Ethical issues are the difficult social questions that involve some level of controversy over what is the right thing to do. Environmental protection is an example of a commonly discussed ethical issue, because there can be tradeoffs between environmental and economic factors.

Ethical dilemmas are situations in which it is difficult for an individual to make decisions either because the right course of action is unclear or carries some potential negative consequences for the person or people involved.

Make no mistake about it: when you enter the business world, you’ll find yourself in situations in which you’ll have to choose the appropriate behavior. How, for example, would you answer questions like the following?

- 1) Is it OK to accept a pair of sports tickets from a supplier?
- 2) Can I buy office supplies from my brother-in-law?
- 3) Is it appropriate to donate company funds to a local charity?
- 4) If I find out that a friend is about to be fired, can I warn her?

Obviously, the types of situations are numerous and varied. Fortunately, we can break them down into a few basic categories: issues of honesty and integrity, conflicts of interest and loyalty, bribes versus gifts, and whistle-blowing. Let's look a little more closely at each of these categories.

Issues of Honesty and Integrity

Master investor Warren Buffet once told a group of business students the following: "I cannot tell you that honesty is the best policy. I can't tell you that if you behave with perfect **honesty** and **integrity** somebody somewhere won't behave the other way and make more money. But honesty is a good policy. You'll do fine, you'll sleep well at night and you'll feel good about the example you are setting for your coworkers and the other people who care about you."¹¹

If you work for a company that settles for its employees' merely obeying the law and following a few internal regulations, you might think about moving on. If you're being asked to deceive customers about the quality or value of your product, you're in an ethically unhealthy environment.

Think about this story:

"A chef put two frogs in a pot of warm soup water. The first frog smelled the onions, recognized the danger, and immediately jumped out. The second frog hesitated: The water felt good, and he decided to stay and relax for a minute. After all, he could always jump out when things got too hot (so to speak). As the water got hotter, however, the frog adapted to it, hardly noticing the change. Before long, of course, he was the main ingredient in frog-leg soup."¹²

Figure 3.2: How to maintain honesty and integrity



So, what's the moral of the story? Don't sit around in an ethically toxic environment and lose your integrity a little at a time; get out before the water gets too hot and your options have evaporated. Fortunately, a few rules of thumb can guide you.

We've summed them up in Figure 3.2 on the previous page.

Conflicts of Interest

Conflicts of interest occur when individuals must choose between taking actions that promote their personal interests over the interests of others or taking actions that don't. A conflict can exist, for example, when an employee's own interests interfere with, or have the potential to interfere with, the best interests of the company's stakeholders (management, customers, and owners). Let's say that you work for a company with a contract to cater events at your college and that your uncle owns a local bakery. Obviously, this situation could create a conflict of interest (or at least give the appearance of one—which is a problem in itself). When you're called on to furnish desserts for a luncheon, you might be tempted to send some business your uncle's way even if it's not in the best interest of your employer. What should you do? You should disclose the connection to your boss, who can then arrange things so that your personal interests don't conflict with the company's.

The same principle holds that an employee shouldn't use private information about an employer for personal financial benefit. Say that you learn from a coworker at your pharmaceutical company that one of its most profitable drugs will be pulled off the market because of dangerous side effects. The recall will severely hurt the company's financial performance and cause its stock price to plummet. Before the news becomes public, you sell all the stock you own in the company. What you've done is called **insider trading** – acting on information that is not available to the general public, either by trading on it or providing it to others who trade on it. Insider trading is illegal, and you could go to jail for it.

Conflicts of Loyalty

You may one day find yourself in a bind between being **loyal** either to your employer or to a friend or family member. Perhaps you just learned that a coworker, a friend of yours, is about to be downsized out of his job. You also happen to know that he and his wife are getting ready to make a deposit on a house near the company headquarters. From a work standpoint,

you know that you shouldn't divulge the information. From a friendship standpoint, though, you feel it's your duty to tell your friend. Wouldn't he tell you if the situation were reversed? So what do you do? As tempting as it is to be loyal to your friend, you shouldn't tell. As an employee, your primary responsibility is to your employer. You might be able to soften your dilemma by convincing a manager with the appropriate authority to tell your friend the bad news before he puts down his deposit.

Bribes versus Gifts

It's not uncommon in business to give and receive small gifts of appreciation, but when is a gift unacceptable? When is it really a **bribe**?

There's often a fine line between a gift and a bribe. The following information may help in drawing it, because it raises key issues in determining how a gesture should be interpreted: the cost of the item, the timing of the gift, the type of gift, and the connection between the giver and the receiver. If you're on the receiving end, it's a good idea to refuse any item that's overly generous or given for the purpose of influencing a decision. Because accepting even small gifts may violate company rules, always check on company policy.

JCPenney's "Statement of Business Ethics," for instance, states that employees can't accept any cash gifts or any noncash gifts except those that have a value below \$50 and that are generally used by the giver for promotional purposes. Employees can attend paid-for business functions, but other forms of entertainment, such as sports events and golf outings, can be accepted only if it's practical for the Penney's employee to reciprocate. Trips of several days can't be accepted under any circumstances.¹³

Whistle-Blowing

As we've seen, the misdeeds of Betty Vinson and her accomplices at WorldCom didn't go undetected. They caught the eye of Cynthia Cooper, the company's director of internal auditing. Cooper, of course, could have looked the other way, but instead she summoned up the courage to be a **whistle-blower**—an individual who exposes illegal or unethical behavior in an organization. Like Vinson, Cooper had majored in accounting at Mississippi State and was a hard-working, dedicated employee. Unlike Vinson, however, she refused to be bullied by her boss, CFO Scott Sullivan. In fact, she had tried to tell not only Sullivan but also auditors from

the Arthur Andersen accounting firm that there was a problem with WorldCom's books. The auditors dismissed her warnings, and when Sullivan angrily told her to drop the matter, she started cleaning out her office. But she didn't relent. She and her team worked late each night, conducting an extensive, secret investigation. Two months later, Cooper had evidence to take to Sullivan, who told her once again to back off. Again, however, she stood up to him, and though she regretted the consequences for her WorldCom coworkers, she reported the scheme to the company's board of directors. Within days, Sullivan was fired and the largest accounting fraud in history became public.¹⁴

As a result of Cooper's actions, executives came clean about the company's financial situation. The conspiracy of fraud was brought to an end, and though public disclosure of WorldCom's problems resulted in massive stock-price declines and employee layoffs, investor and employee losses would have been greater without Cooper's intervention. Even though Cooper did the right thing, and landed on the cover of *Time* magazine for it, the experience wasn't exactly gratifying.

A lot of people applauded her action, but many coworkers shunned her; some even blamed her for the company's troubles.¹⁵

Whistle-blowing is sometimes career suicide. A survey of two hundred whistle-blowers conducted by the National Whistleblower Center found that half were fired for blowing the whistle.¹⁶ Even those who keep their jobs can experience repercussions. As long as they stay, some will treat them (as one whistle-blower put it) "like skunks at a picnic"; if they leave, they may be blackballed in the industry.¹⁷ On a positive note, new Federal laws have been passed which are intended to protect whistle-blowers.

For her own part, Cynthia Cooper doesn't regret what she did. As she told a group of students at Mississippi State: "Strive to be persons of honor and integrity. Do not allow yourself to be pressured. Do what you know is right even if there may be a price to be paid."¹⁸ If your company tells employees to do whatever it takes, push the envelope, look the other way, and "be sure that we make our numbers," you have three choices: go along with the policy, try to change things, or leave. If your personal integrity is part of the equation, you're probably down to the last two choices.¹⁹

Corporate Social Responsibility

Corporate social responsibility refers to the approach that an organization takes in balancing its responsibilities toward different stakeholders when making legal, economic, ethical, and social decisions. Remember that we previously defined **stakeholders** as those with a legitimate interest in the success or failure of the business and the policies it adopts. The term social responsibility refers to the approach that an organization takes in balancing its responsibilities toward their various stakeholders.

What motivates companies to be “socially responsible”? We hope it’s because they want to do the right thing, and for many companies, “doing the right thing” is a key motivator. The fact is, it’s often hard to figure out what the “right thing” is: what’s “right” for one group of stakeholders isn’t necessarily just as “right” for another. One thing, however, is certain: companies today are held to higher standards than ever before. Consumers and other groups consider not only the quality and price of a company’s products but also its character. If too many groups see a company as a poor corporate citizen, it will have a harder time attracting qualified employees, finding investors, and selling its products. Good corporate citizens, by contrast, are more successful in all these areas.

Figure 3.3 presents a model of corporate responsibility based on a company’s relationships with its stakeholders. In this model, the focus is on **managers**—not owners—as the principals involved in these relationships. **Owners** are the stakeholders who invest risk capital in the firm in expectation of a financial return. Other stakeholders include **employees**, **suppliers**, and the **communities** in which the firm does business. Proponents of this model hold that customers, who provide the firm with revenue, have a special claim on managers’ attention. The arrows indicate the two-way nature of corporation-stakeholder relationships: All stakeholders have some claim on the firm’s resources and returns, and management’s job is to make decisions that balance these claims.²⁰

Let's look at some of the ways in which companies can be "socially responsible" in considering the claims of various stakeholders.

Figure 3.3: Management's relationships with stakeholders



Owners

Owners invest money in companies. In return, the people who run a company have a responsibility to increase the value of owners' investments through profitable operations. Managers also have a responsibility to provide owners (as well as other stakeholders having financial interests, such as creditors and suppliers) with accurate, reliable information about the performance of the business. Clearly, this is one of the areas in which WorldCom managers fell down on the job. Upper-level management purposely deceived shareholders by presenting them with fraudulent financial statements

Managers

Managers have what is known as a fiduciary responsibility to owners: they're responsible for safeguarding the company's assets and handling its funds in a trustworthy manner. Yet managers experience what is called the agency problem; a situation in which their best interests do not align with those of the owners who employ them. To enforce managers' fiduciary responsibilities for a firm's financial statements and accounting records, the Sarbanes-Oxley Act of 2002 requires CEOs and CFOs to attest to their accuracy. The law also imposes penalties on corporate officers, auditors, board members, and any others who commit fraud. You'll learn more about this law in your accounting and business law courses.

Employees

Companies are responsible for providing **employees** with safe, healthy places to work—as well as environments that are free from sexual harassment and all types of discrimination. They should also offer appropriate wages and benefits. In the following sections, we'll take a closer look at these areas of corporate responsibility.

Wages and Benefits

At the very least, employers must obey laws governing minimum wage and overtime pay. A **minimum wage** is set by the federal government, though states can set their own rates as long as they are higher. The current federal rate, for example, is \$7.25, while the rate in many states is far higher.²¹ By law, employers must also provide certain **benefits**—social security (retirement funds), unemployment insurance (protects against loss of income in case of job loss), and workers' compensation (covers lost wages and medical costs in case of on-the-job injury). Most large companies pay most of their workers more than minimum wage and offer broader benefits, including medical, dental, and vision care, as well as savings programs, in order to compete for talent.

Safety and Health

Though it seems obvious that companies should guard workers' **safety and health**, some simply don't. For over four decades, for example, executives at Johns Manville suppressed evidence that one of its products, asbestos, was responsible for the deadly lung disease developed by many of its workers.²² The company concealed chest X-rays from stricken workers, and executives decided that it was simply cheaper to pay workers' compensation claims than to create a safer work environment. A New Jersey court was quite blunt in its judgment: Johns Manville, it held, had made a deliberate, cold-blooded decision to do nothing to protect at-risk workers, in blatant disregard of their rights.²³

About four in one hundred thousand U.S. workers die in workplace "incidents" each year. The Department of Labor categorizes deaths caused by conditions like those at Johns Manville as "exposure to harmful substances or environments." How prevalent is this condition as a cause of workplace deaths? See Figure 3.4, "Workplace Deaths by Event or Exposure, 2014", which breaks down workplace fatalities by cause. Some jobs are more dangerous than others. For a comparative overview based on workplace deaths by occupation, see Figure 3.5.

Fortunately for most people, things are far better than they were at Johns Manville. Procter & Gamble (P&G), for example, considers the safety and health of its employees paramount and promotes the attitude that "Nothing we do is worth getting hurt for." With nearly one hundred thousand employees worldwide, P&G uses a measure of worker safety called "total incident rate per employee," which records injuries resulting in loss of consciousness, time lost from work, medical transfer to another job, motion restriction, or medical treatment beyond first aid. The company attributes the low rate of such incidents—less than one incident per hundred employees—to a variety of programs to promote workplace safety.²⁴

Figure 3.4: Workplace deaths by event or exposure, 2014.

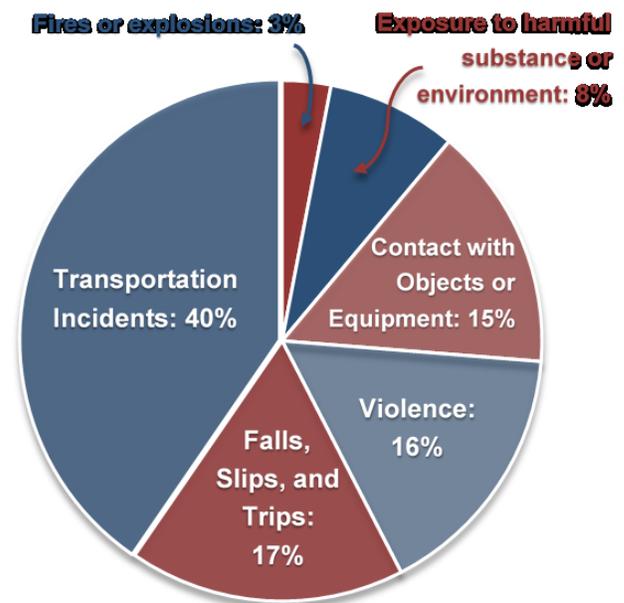


Figure 3.5: Workplace deaths by occupation, 2014.

Industry	% of Total Workplace Deaths
Construction	19%
Transportation and Warehousing	16%
Agriculture, Forestry, and Fishing	12%
Government	9%
Professional and Business Services	9%
Manufacturing	7%
Retail Trade	6%
Leisure and Hospitality	4%
Mining, Quarrying, and Natural Gas Extraction	4%

Customers

The purpose of any business is to satisfy **customers**, who reward businesses by buying their products. Sellers are also responsible—both ethically and legally—for treating customers fairly. The rights of consumers were first articulated by President John F. Kennedy in 1962 when he submitted to Congress a presidential message devoted to consumer issues.²⁵ Kennedy identified four consumer rights:

- 1) **The right to safe products.** A company should sell no product that it suspects of being unsafe for buyers. Thus, producers have an obligation to safety-test products before releasing them for public consumption. The automobile industry, for example, conducts extensive safety testing before introducing new models (though recalls remain common).
- 2) **The right to be informed about a product.** Sellers should furnish consumers with the product information that they need to make an informed purchase decision. That's why pillows have labels identifying the materials used to make them, for instance.
- 3) **The right to choose what to buy.** Consumers have a right to decide which products to purchase, and sellers should let them know what their options are. Pharmacists, for example, should tell patients when a prescription can be filled with a cheaper brand-name or generic drug. Telephone companies should explain alternative calling plans.

- 4) **The right to be heard.** Companies must tell customers how to contact them with complaints or concerns. They should also listen and respond.

Companies share the responsibility for the legal and ethical treatment of consumers with several government agencies: the **Federal Trade Commission** (FTC), which enforces consumer-protection laws; the **Food and Drug Administration** (FDA), which oversees the labeling of food products; and the **Consumer Product Safety Commission**, which enforces laws protecting consumers from the risk of product-related injury.

Communities

For obvious reasons, most **communities** see getting a new business as an asset and view losing one—especially a large employer—as a detriment. After all, the economic impact of business activities on local communities is substantial: They provide jobs, pay taxes, and support local education, health, and recreation programs. Both big and small businesses donate funds to community projects, encourage employees to volunteer their time, and donate equipment and products for a variety of activities. Larger companies can make greater financial contributions. Let's start by taking a quick look at the philanthropic activities of a few U.S. corporations.

Philanthropy

Many large corporations support various charities, an activity called **philanthropy**. Some donate a percentage of sales or profits to worthwhile causes. Retailer Target, for example, donates 5 percent of its profits—about \$2 million per week—to schools, neighborhoods, and local projects across the country; its store-based grants underwrite programs in early childhood education, the arts, and family-violence prevention.²⁶ The late actor Paul Newman donated 100 percent of the profits from “Newman’s Own” foods (salad dressing, pasta sauce, popcorn, and other products sold in eight countries). His company continues his legacy of donating all profits and distributing them to thousands of organizations, including the Hole in the Wall Gang camps for seriously ill children.²⁷

Ethical Organizations

How Can You Recognize an Ethical Organization?

One goal of anyone engaged in business should be to foster **ethical behavior** in the organizational environment. How do we know when an organization is behaving ethically? Most lists of ethical organizational activities include the following criteria:

- Treating employees, customers, investors, and the public fairly
- Holding every member personally accountable for his or her action
- Communicating core values and principles to all members
- Demanding and rewarding integrity from all members in all situations²⁸

Employees at companies that consistently make Business Ethics magazine's list of the "100 Best Corporate Citizens" regard the items on the previous list as business as usual in the workplace. Companies at the top of the 2016 list include Microsoft, Hasbro, Ecolab, Bristol-Myers-Squibb, and Lockheed Martin.²⁹

By contrast, employees with the following attitudes tend to suspect that their employers aren't as ethical as they should be:

- They consistently feel uneasy about the work they do.
- They object to the way they're treated.
- They're uncomfortable about the way coworkers are treated.
- They question the appropriateness of management directives and policies.³⁰

Sexual Harassment

Sexual harassment occurs when an employee makes "unwelcome sexual advances, requests for sexual favors, and other verbal or physical conduct of a sexual nature" to another employee. It's also considered sexual harassment when "submission to or rejection of this conduct explicitly or implicitly affects an individual's employment, unreasonably interferes with an individual's work performance or creates an intimidating, hostile or offensive work environment."³¹

To prevent sexual harassment—or at least minimize its likelihood—a company should adopt a formal anti-harassment **policy** describing prohibited conduct, asserting its objections to the behavior, and detailing penalties for violating the policy.³² Employers also have an obligation to investigate harassment complaints. Failure to enforce anti-harassment policies can be very costly. In 1998, for example, Mitsubishi paid \$34 million to more than three hundred fifty female employees of its Normal, Illinois, plant to settle a sexual harassment case supported by the **Equal Employment Opportunity Commission**. The EEOC reprimanded the company for permitting an atmosphere of verbal and physical abuse against women, charging that female workers had been subjected to various forms of harassment, ranging from exposure to obscene graffiti and vulgar jokes to fondling and groping.³³

Workforce Diversity

In addition to complying with equal employment opportunity laws, many companies make special efforts to recruit employees who are underrepresented in the workforce according to sex, race, or some other characteristic. In helping to build more **diverse** workforces, such initiatives contribute to competitive advantage for two reasons:

- 1) People from diverse backgrounds bring new talents and fresh perspectives to an organization, typically enhancing creativity in the development of new products.
- 2) By more accurately reflecting the demographics of the marketplace, a diverse workforce improves a company's ability to serve an ethnically diverse population.

The Individual Approach to Ethics

Betty Vinson didn't start out at WorldCom with the intention of going to jail. She undoubtedly knew what the right behavior was, but the bottom line is that she didn't do it. How can you make sure that you do the right thing in the business world? How should you respond to the kinds of challenges that you'll be facing? Because your actions in the business world will be strongly influenced by your moral character, let's begin by assessing your current moral condition. Which of the following best applies to you (select one)?

- 1) I'm always ethical.
- 2) I'm mostly ethical.
- 3) I'm somewhat ethical.
- 4) I'm seldom ethical.
- 5) I'm never ethical.

Now that you've placed yourself in one of these categories, here are some general observations. Few people put themselves below the second category. Most of us are ethical most of the time, and most people assign themselves to category number two— "I'm mostly ethical." Why don't more people claim that they're always ethical?

Apparently, most people realize that being ethical all the time takes a great deal of moral energy. If you placed yourself in category number two, ask yourself this question: How can I change my behavior so that I can move up a notch? The answer to this question may be simple. Just ask yourself an easier question: How would I like to be treated in a given situation?³⁴

Unfortunately, practicing this philosophy might be easier in your personal life than in the business world. Ethical challenges arise in business because companies, especially large ones, have multiple stakeholders who sometimes make competing demands. Making decisions that affect multiple stakeholders isn't easy even for seasoned managers; and for new entrants to the business world, the task can be extremely daunting. You can, however, get a head start in learning how to make ethical decisions by looking at two types of challenges that you'll encounter in the business world: ethical dilemmas and ethical decisions.

Addressing Ethical Dilemmas

An **ethical dilemma** is a morally problematic situation: you must choose between two or more acceptable but often opposing alternatives that are important to different groups. Experts often frame this type of situation as a "right-versus-right" decision. It's the sort of decision that Johnson & Johnson (known as J&J) CEO James Burke had to make in 1982.³⁵ On September 30, twelve-year-old Mary Kellerman of Chicago died after her parents gave her Extra-Strength Tylenol. That same morning, twenty-seven-year-old Adam Janus, also of Chicago, died after taking Tylenol for minor chest pain. That night, when family members came to console his parents, Adam's brother and his wife took Tylenol from the same bottle and died within forty-

eight hours. Over the next two weeks, four more people in Chicago died after taking Tylenol. The actual connection between Tylenol and the series of deaths wasn't made until an off-duty fireman realized from news reports that every victim had taken Tylenol. As consumers panicked, J&J pulled Tylenol off Chicago-area retail shelves. Researchers discovered Tylenol capsules containing large amounts of deadly cyanide. Because the poisoned bottles came from batches originating at different J&J plants, investigators determined that the tampering had occurred after the product had been shipped.³⁶

So J&J wasn't at fault. But CEO Burke was still faced with an extremely serious dilemma: Was it possible to respond to the tampering cases without destroying the reputation of a highly profitable brand?

Burke had two options:

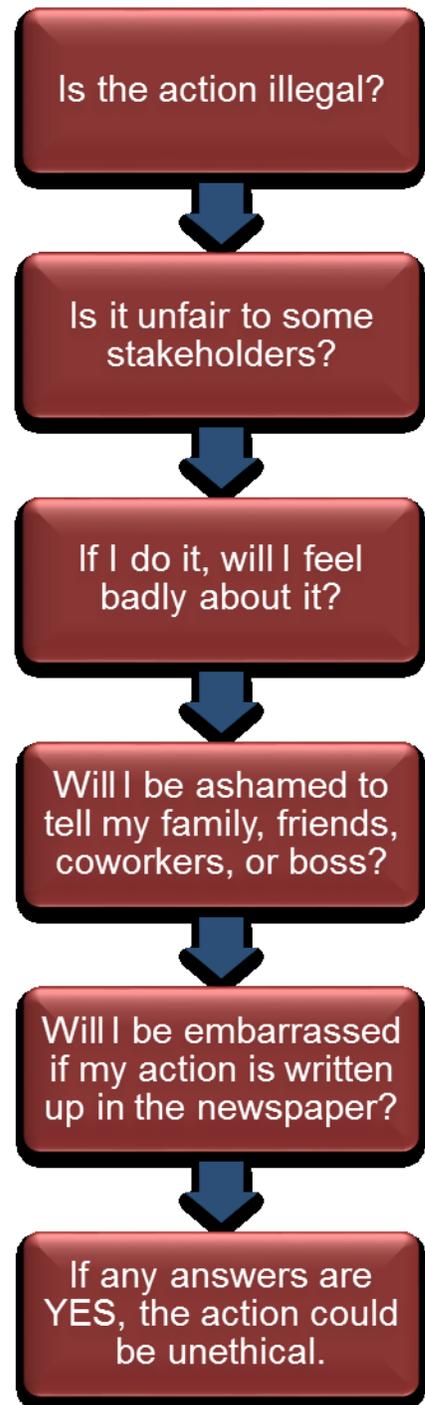
- 1) He could recall only the lots of Extra-Strength Tylenol that were found to be tainted with cyanide. In 1991, Perrier executives recalled only tainted product when they discovered that cases of their bottled water had been poisoned with benzene. This option favored J&J financially but possibly put more people at risk.
- 2) Burke could order a nationwide recall—of all bottles of Extra-Strength Tylenol. This option would reverse the priority of the stakeholders, putting the safety of the public above stakeholders' financial interests.

Burke opted to recall all 31 million bottles of Extra-Strength Tylenol on the market. The cost to J&J was \$100 million, but public reaction was quite positive. Less than six weeks after the crisis began, Tylenol capsules were reintroduced in new tamper-resistant bottles, and by responding quickly and appropriately, J&J was eventually able to restore the Tylenol brand to its previous market position. When Burke was applauded for moral courage, he replied that he'd simply adhered to the long-standing J&J credo that put the interests of customers above those of other stakeholders. His only regret was that the perpetrator was never caught.³⁷

If you're wondering what your thought process should be if you're confronted with an ethical dilemma, you might wish to remember the mental steps listed here—which happen to be the steps that James Burke took in addressing the Tylenol crisis:

- 1) **Define the problem:** How to respond to the tampering case without destroying the reputation of the Tylenol brand.
- 2) **Identify feasible options:** (1) Recall only the lots of Tylenol that were found to be tainted or (2) order a nationwide recall of all bottles of Extra-Strength Tylenol.
- 3) **Assess the effect of each option on stakeholders:** Option 1 (recalling only the tainted lots of Tylenol) is cheaper but puts more people at risk. Option 2 (recalling all bottles of Extra-Strength Tylenol) puts the safety of the public above stakeholders' financial interests.
- 4) **Establish criteria for determining the most appropriate action:** Adhere to the J&J credo, which puts the interests of customers above those of other stakeholders.
- 5) **Select the best option based on the established criteria:** In 1982, Option 2 was selected, and a nationwide recall of all bottles of Extra-Strength Tylenol was conducted.

Figure 3.6: How to avoid an ethical lapse: questions to ask



Making Ethical Decisions

In contrast to the “right-versus-right” problem posed by an ethical dilemma, an **ethical decision** entails a “right-versus-wrong” decision—one in which there is clearly a right (ethical) choice and a wrong (unethical or illegal) choice. When you make a decision that’s unmistakably unethical or illegal, you’ve committed an ethical lapse. If you’re presented with this type of choice, asking yourself the questions in Figure 3.6 “How to Avoid an Ethical Lapse” will increase your odds of making an ethical decision.

To test the validity of this approach, let's take a point-by-point look at Betty Vinson's decisions:

- 1) Her actions were clearly illegal.
- 2) They were unfair to the workers who lost their jobs and to the investors who suffered financial losses (and also to her family, who shared her public embarrassment).
- 3) She definitely felt badly about what she'd done.
- 4) She was embarrassed to tell other people what she had done.
- 5) Reports of her actions appeared in her local newspaper (and just about every other newspaper in the country).

So Vinson could have answered “yes” to all five of our test questions. To simplify matters, remember the following rule of thumb: If you answer yes to any one of these five questions, odds are that you're about to do something you shouldn't.

Revisiting Johnson & Johnson

As discussed earlier, Johnson & Johnson received tremendous praise for the actions taken by its CEO, James Burke, in response to the 1982 Tylenol catastrophe. However, things change. To learn how a company can destroy its good **reputation**, let's fast forward to 2008 and revisit J&J and its credo, which states, “We believe our first responsibility is to the doctors, nurses and patients, to mothers and fathers and all others who use our products and services. In meeting their needs everything we do must be of high quality.”³⁸ How could a company whose employees believed so strongly in its credo find itself under criminal and congressional investigation for a series of recalls due to defective products?³⁹ In a three-year period, the company recalled twenty-four products, including Children's, Infants' and Adults' Tylenol, Motrin, and Benadryl;⁴⁰ 1-Day Acuvue TruEye contact lenses sold outside the U.S.,⁴¹ and hip replacements.⁴²

Unlike the Tylenol recall, no one had died from the defective products, but customers were certainly upset to find they had purchased over-the-counter medicines for themselves and their children that were potentially contaminated with dark particles or tiny specks of metal;⁴³ contact lenses that contained a type of acid that caused stinging or pain when inserted in the eye;⁴⁴ and defective hip implants that required patients to undergo a second hip replacement.⁴⁵

Who bears the responsibility for these image-damaging blunders? Two individuals who were at least partially responsible were William Weldon, CEO, and Colleen Goggins, Worldwide Chairman of J&J's Consumer Group. Weldon has been criticized for being largely invisible and publicly absent during the recalls.⁴⁶ Additionally, he admitted that he did not understand the consumer division where many of the quality control problems originated.⁴⁷ Goggins was in charge of the factories that produced many of the recalled products. She was heavily criticized by fellow employees for her excessive cost-cutting measures and her propensity to replace experienced scientists with new hires.⁴⁸ In addition, she was implicated in scheme to avoid publically disclosing another J&J recall of a defective product.

After learning that J&J had released packets of Motrin that did not dissolve correctly, the company hired contractors to go into convenience stores and secretly buy up every pack of Motrin on the shelves. The instructions given to the contractors were the following: "You should simply 'act' like a regular customer while making these purchases. THERE MUST BE NO MENTION OF THIS BEING A RECALL OF THE PRODUCT!"⁴⁹ In May 2010, when Goggins appeared before a congressional committee investigating the "phantom recall," she testified that she was not aware of the behavior of the contractors⁵⁰ and that she had "no knowledge of instructions to contractors involved in the phantom recall to not tell store employees what they were doing." In her September 2010 testimony to the House Committee on Oversight and Government Reform, she acknowledged that the company in fact wrote those very instructions.

Refusing to Rationalize

Despite all the good arguments in favor of doing the right thing, why do many reasonable people act unethically (at least at times)? Why do good people make bad choices? According to one study, there are four common **rationalizations** (excuses) for justifying misconduct:⁵¹

- 1) **My behavior isn't really illegal or immoral.** Rationalizers try to convince themselves that an action is OK if it isn't downright illegal or blatantly immoral. They tend to operate in a gray area where there's no clear evidence that the action is wrong.

- 2) **My action is in everyone's best interests.** Some rationalizers tell themselves: "I know I lied to make the deal, but it'll bring in a lot of business and pay a lot of bills." They convince themselves that they're expected to act in a certain way.⁵²
- 3) **No one will find out what I've done.** Here, the self-questioning comes down to "If I didn't get caught, did I really do it?" The answer is yes. There's a simple way to avoid succumbing to this rationalization: Always act as if you're being watched.
- 4) **The company will condone my action and protect me.** This justification rests on a fallacy. Betty Vinson may honestly have believed that her actions were for the good of the company and that her boss would, therefore, accept full responsibility (as he promised). When she goes to jail, however, she'll go on her own.

Here's another rule of thumb: If you find yourself having to rationalize a decision, it's probably a bad one.

Figure 3.7

What to Do When the Light Turns Yellow

Like our five questions, some ethical problems are fairly straightforward. Others, unfortunately, are more complicated, but it will help to think of our five-question test as a set of signals that will warn you that you're facing a particularly tough decision—that you should think carefully about it and perhaps consult someone else. The situation is like approaching a traffic light. Red and green lights are easy; you know what they mean and exactly what to do. Yellow lights are trickier. Before you decide which pedal to hit, try posing our five questions. If you get a single yes, you'll almost surely be better off hitting the brake.⁵³



Key Take-Aways

- 1) Business ethics is the application of ethical behavior in a business context. Ethical (trustworthy) companies are better able to attract and keep customers, talented employees, and capital.
- 2) Acting ethically in business means more than just obeying laws and regulations. It also means being honest, doing no harm to others, competing fairly, and declining to put your own interests above those of your employer and coworkers.
- 3) In the business world, you'll encounter conflicts of interest: situations in which you'll have to choose between taking action that promotes your personal interest and action that favors the interest of others.
- 4) Corporate social responsibility refers to the approach that an organization takes in balancing its responsibilities toward different stakeholders (owners, employees, customers, and the communities in which they conduct business) when making legal, economic, ethical, and social decisions.
- 5) Managers have several responsibilities: to increase the value of owners' investments through profitable operations, to provide owners and other stakeholders with accurate, reliable financial information, and to safeguard the company's assets and handle its funds in a trustworthy manner.

Key Take-Aways

- 6) Companies have a responsibility to pay appropriate wages and benefits, treat all workers fairly, and provide equal opportunities for all employees. In addition, they must guard workers' safety and health and to provide them with a work environment that's free from sexual harassment.
- 7) Consumers have certain legal rights: to use safe products, to be informed about products, to choose what to buy, and to be heard. Sellers must comply with these requirements.
- 8) Businesspeople face two types of ethical challenges: ethical dilemmas and ethical decisions.
- 9) An ethical dilemma is a morally problematic situation in which you must choose competing and often conflicting options which do not satisfy all stakeholders.
- 10) An ethical decision is one in which there's a right (ethical) choice and a wrong (unethical or downright illegal) choice.

Chapter 3 Text References and Image Credits

Image Credits: Chapter 3

Figure 3.1: “Bernie Madoff’s Mug Shot.” U.S. Department of Justice, public domain. Retrieved from: https://en.wikipedia.org/wiki/Bernard_Madoff#/media/File:BernardMadoff.jpg

Figure 3.4: “Workplace deaths by event or exposure, 2014.” Data retrieved from: Bureau of Labor Statistics: <http://www.bls.gov/iif/oshwc/cfoi/cfch0013.pdf> (p. 3).

Figure 3.5: “Workplace deaths by occupation, 2014.” Data retrieved from: Bureau of Labor Statistics: <http://www.bls.gov/iif/oshwc/cfoi/cfch0013.pdf> (p. 13).

Figure 3.7: Yellow traffic light. Sir James (2009). “Traffic light modern version Ireland Dublin.” [Creative Commons Attribution-Share Alike 3.0 Unported](https://commons.wikimedia.org/wiki/File:Traffic_light_modern_version_Ireland_Dublin_2_yellow_2009-09-27.jpg). Retrieved from: https://commons.wikimedia.org/wiki/File:Traffic_light_modern_version_Ireland_Dublin_2_yellow_2009-09-27.jpg

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