

CROSS • MILLER

The
LEGAL
ENVIRONMENT
of BUSINESS

TEXT AND CASES



ELEVENTH EDITION

Chapter 3

Ethics in Business

3-1 Ethics and the Role of Business

- **Ethics** – Moral principles and values applied to social behavior.
 - Ethics has to do with an action's:
 - Fairness
 - Justness
 - Rightness
 - Wrongness
- **Business ethics** – Ethics in a business context; a consensus of what constitutes right or wrong behavior in the world of business and the application of moral principles to situations that arise in a business setting.

3-1a The Relationship of Law and Ethics (slide 1 of 3)

- The government has institutionalized some ethical rights and duties through the passage of laws and regulations.
- Many laws are designed to prevent fraudulent (misleading, deceptive) conduct in various contexts, including:
 - Contracts
 - Health care
 - Financial reporting
 - Mortgages
 - Sales
- Sometimes, major legislation is passed after well-publicized ethical transgressions by industries or companies result in harm to the public.

3-1a The Relationship of Law and Ethics (slide 2 of 3)

Gray Areas in the Law

- Laws cannot codify all ethical requirements.
- Laws may sometimes be difficult to interpret and apply due to a number of reasons, including:
 - Broad language
 - Application of a law to more than just the intended situation
 - Unclear guidance on the purpose of a law
 - Ambiguous or weak provisions

The Moral Minimum

- **Moral minimum** – The minimum degree of ethical behavior expected of a business firm, which is usually defined as compliance with the law.
- Businesspersons must remember that an action that is legal is not necessarily ethical.

3-1a The Relationship of Law and Ethics (slide 3 of 3)

Private Company Codes of Ethics

- Most companies attempt to link ethics and law through the creation of internal codes of ethics.
- Company codes are not laws.
 - Instead, they are rules that the company sets forth and that it can enforce.
- Codes of conduct typically outline the company's policies on particular issues and indicate how employees are expected to act.

Industry Ethical Codes

- Numerous industries have developed codes of ethics.
- Violation of a code may result in the discipline of an employee or sanctions against a company from the industry organization.
- Internal codes are not laws, so their effectiveness is determined by the commitment of the industry or company leadership enforcing them.

3-1b The Role of Business in Society (slide 1 of 3)

Business as a Pure Profit Maximizer

- Originally, the only perceived duty of a corporation was to maximize profits and generate revenues for its owners.
 - Although many people today may view this idea as greedy or ruthless, the rationale for the profit-maximization theory is still valid.
- In theory, if all firms strictly adhered to the goal of maximizing profits, it would lead to the most efficient allocation of scarce resources.

3-1b The Role of Business in Society (slide 2 of 3)

Business as a Corporate Citizen

- Over the years, many people became dissatisfied with the profit-maximization theory, and corporations came to be viewed as “citizens” that were expected to participate in bettering communities and society.
- **Triple bottom line** – The idea that investors and others should consider not only corporate profits, but also the corporation’s impact on people and on the planet in assessing the firm.
 - The bottom line is:
 - People
 - Planet
 - Profits

3-1b The Role of Business in Society (slide 3 of 3)

A Four-Part Analysis

- When making decisions, a business should evaluate each of the following:
 1. The legal implications of each decision
 2. The public relations impact
 3. The safety risks for consumers and employees
 4. The financial implications
- This four-part analysis will assist the firm in making decisions that not only maximize profits but also reflect good corporate citizenship.

3-1c Ethical Issues in Business (slide 1 of 2)

- A fundamental ethical issue for business is developing integrity and trust.
 - Businesspersons should exhibit integrity in their dealings with:
 - Other people in the company
 - Other businesses
 - Clients
 - The community
- Businesses should also ensure that the workplace respects diversity and enforces equal opportunity employment and civil rights laws.

3-1c Ethical Issues in Business (slide 2 of 2)

- Businesses must comply with a host of federal and state laws and regulations, including those pertaining to:
 - The environment
 - Financial reporting
 - Safety standards
- The most difficult aspect of ethics that businesses face is in decision making.
 - Businesspersons must learn to:
 1. Recognize ethical issues
 2. Get the pertinent facts
 3. Evaluate the alternatives
 4. Make a decision
 5. Test and reflect on the outcome of their decision

3-1d The Importance of Ethical Leadership

Attitude of Top Management

- One of the most important ways to create and maintain an ethical workplace is for top management to demonstrate its commitment to ethical decision making.
 - Top management's behavior sets the ethical tone of a firm.

Unrealistic Goals for Employees

- Managers who set unrealistic production or sales goals increase the probability that employees will act unethically.

Fostering of Unethical Conduct

- Business owners and managers sometimes take more active roles in fostering unethical and illegal conduct, with negative consequences for their businesses.

3-2 Ethical Principles and Philosophies

- **Ethical reasoning** – A reasoning process in which an individual links his or her moral convictions or ethical standards to the particular situation at hand.
 - Ethical reasoning applies to businesses as well.
 - As businesses make decisions, they must consider the ethical implications of each alternative.
- The study of ethics identifies two major categories:
 1. **Duty-based ethics** – An ethical philosophy rooted in the idea that every person has certain duties to others, including both humans and the planet.
 - Those duties may be derived from religious principles or from other philosophical reasoning.
 2. **Outcome-based ethics** – An ethical philosophy that focuses on the impacts of a decision on society or on key stakeholders.

3-2a Duty-Based Ethics (slide 1 of 4)

- Duty-based ethics deals with standards for behavior that traditionally were derived from:
 - Revealed truths
 - Religious authorities
 - Philosophical reasoning
- These standards involve concepts of:
 - Right and wrong
 - Duties owed
 - Rights to be protected

3-2a Duty-Based Ethics (slide 2 of 4)

Religious Ethical Principles

- Nearly every religion has principles or beliefs about how one should treat others.
 - **Examples:** The Ten Commandments, the Qur'an, the four Vedas
- Religious rules generally are absolute with respect to the behavior of their adherents.
- For businesses, religious principles can be a unifying force for employees or a rallying point to increase employee motivation.
- They can also present problems, however, because different owners, suppliers, employees, and customers may have different religious backgrounds.

3-2a Duty-Based Ethics (slide 3 of 4)

Principles of Rights

- **Principle of rights** – The principle that human beings have certain fundamental rights (to life, freedom, and the pursuit of happiness, for example).
 - A key factor in determining whether a business decision is ethical under this theory is how that decision affects the rights of others, such as employees, customers, suppliers, and the community.
- A potential dilemma for those who support rights theory is that they may disagree on which rights are most important.
 - In general, rights theorists believe that whichever right is stronger in a particular circumstance takes precedence.

3-2a Duty-Based Ethics (slide 4 of 4)

Kantian Ethical Principles

- The German philosopher Immanuel Kant (1724–1804) believed that human beings are:
 - Qualitatively different from other physical objects
 - Endowed with moral integrity and the capacity to reason and conduct their affairs rationally
- Based on this view, Kant said that when people are treated merely as a means to an end (such as when employees are treated as profit-making tools), they are being treated as the equivalent of objects and are being denied their basic humanity.
- A central postulate of Kantian ethics is the categorical imperative.
 - **Categorical imperative** – In deciding whether an action is right or wrong, or desirable or undesirable, a person should evaluate the action in terms of what would happen if everybody else in the same situation, or category, acted the same way.

3-2b Outcome-Based Ethics: Utilitarianism

(slide 1 of 2)

- Outcome-based ethics:
 - Focuses on the consequences of an action rather than on the nature of the action itself or any set of preestablished moral values or religious beliefs
 - Looks at the impacts of a decision in an attempt to maximize benefits and minimize harms
- The premier philosophical theory for outcome-based decision making is utilitarianism.
 - **Utilitarianism** – An approach to ethical reasoning in which ethically correct behavior is related to an evaluation of the consequences of a given action on those who will be affected by it.
 - In utilitarian reasoning, a “good” decision is one that results in the greatest good for the greatest number of people affected by the decision.

3-2b Outcome-Based Ethics: Utilitarianism

(slide 2 of 2)

Cost-Benefit Analysis

- Applying the utilitarian theory requires the following steps:
 1. A determination of which individuals will be affected by the action in question
 2. A cost-benefit analysis
 - **Cost-benefit analysis** – A decision-making technique that involves weighing the costs of a given action against the benefits of the action.
 3. A choice among alternative actions that will produce maximum societal utility (the greatest positive net benefits for the greatest number of individuals)

Problems with the Utilitarian Approach

- In some situations, an action that produces the greatest good for the most people may not seem to be the most ethical.

3-2c Corporate Social Responsibility (slide 1 of 4)

- **Corporate social responsibility (CSR)** – The concept that corporations can and should act ethically and be accountable to society for their actions.
- CSR is not imposed on corporations by law.
 - However, it does involve a commitment to self-regulation in a way that attends to the text and intent of the law as well as to ethical norms and global standards.
- CSR is most successful when a company undertakes activities that are significant and related to its business operations.
- Some types of CSR activities that businesses are engaging in today include:
 1. Environmental efforts
 2. Ethical labor practices
 3. Charitable donations
 4. Volunteer work

3-2c Corporate Social Responsibility (slide 2 of 4)

The Corporate Aspects of CSR

- Arguably, any socially responsible activity will benefit a corporation.
 - Benefits can include:
 - An increase in goodwill from the local community
 - An increase in sales
 - Higher employee retention
 - At times, the benefit may not be immediate.
 - **Example:** The high initial costs of the construction of a plant to meet high energy and environmental standards offset by the savings in maintenance and utilities over the life of the building

3-2c Corporate Social Responsibility (slide 3 of 4)

The Social Aspects of CSR

- Because business controls so much of the wealth and power in this country, business has a responsibility to use that wealth and power in socially beneficial ways.
- The social aspects of CSR require corporations to demonstrate that they are:
 - Promoting goals that society deems worthwhile
 - Moving toward solutions to social problems
- Companies may be judged on:
 - How much they donate to social causes
 - How they conduct their operations with respect to employment discrimination, human rights, environmental concerns, and similar issues

3-2c Corporate Social Responsibility (slide 4 of 4)

Stakeholders and CSR

- One view of CSR stresses that corporations have a duty to both shareholders and stakeholders.
 - **Stakeholders** – Groups, other than the company's shareholders, that are affected by corporate decisions.
 - Stakeholders include:
 - Employees
 - Customers
 - Suppliers
 - The community in which the corporation operates
- The rationale for this view is that, in some circumstances, one or more of these groups may have a greater stake in company decisions than the shareholders do.

3-3 Sources of Ethical Issues in Business Decisions

- A key to avoiding unethical conduct is to recognize how certain situations may lead individuals to act unethically.

3-3a Short-Term Profit Maximization

- In attempting to maximize profits, corporate executives and employees have to distinguish between short-run and long-run profit maximization.
 - **Example:** Continuing to sell a defective product to increase profits (short-run profit maximization) versus lawsuits, large settlements, and bad publicity as a result of continuing to sell the product (long-run profit maximization)
- An overemphasis on short-run profit maximization is perhaps the most common reason that ethical problems occur in business.

3-3b Social Media

- Businesses often face ethical issues with respect to social media platforms (e.g., Facebook, Twitter, Snapchat, Pinterest, etc.).

The Use of Social Media to Make Hiring Decisions

- Employers are likely to use social media to evaluate job candidates.
 - Many people feel that judging a job candidate on what she or he does outside the work environment is unethical.

The Use of Social Media to Discuss Work-Related Issues

- Until recently, companies were free to discipline or even fire employees for their behavior on social media sites.
- The National Labor Relations Board (NLRB) ruled that an employer cannot broadly prohibit its employees from criticizing the company or co-workers, supervisors, or managers via social media.

3-3c Awareness

- Regardless of the context in which a decision is called for, sometimes businesspersons are not even aware that the decision has ethical implications.

3-3d Rationalization

- Sometimes, businesspersons rationalize ethically questionable decisions.
 - **Example:** An employee might rationalize it is acceptable to take company property for personal use just this one time, because she or he normally does not act in this way.
- To counteract rationalization, businesspersons should first decide the right thing to do on an ethical level before making a business decision, then figure out how to mitigate the costs of doing the right thing.

3-3e Uncertainty

- One common denominator identified by businesspersons who have faced ethical problems is the feeling of uncertainty about what they should do, what they should have done, or whether there was an ethical issue or ethical breach involved.
 - Such uncertainty is practically unavoidable, but it should be treated as an indicator of a potential ethical problem.
 - When this occurs, a decision maker should:
 1. Try to identify what the ethical dilemma is
 2. Try to identify why he or she is feeling uneasy
 3. Take the time to think through the decision completely
 4. Consider various options

3-4 Making Ethical Business Decisions

- Several frameworks exist to help businesspersons make ethical decisions.
 - One such framework is a modified version of ethics consultant Leonard H. Bucklin's Business Process Pragmatism™ procedure, called IDDR ("I Desire to Do Right").

3-4a A Systematic Approach: IDDR (“I Desire to Do Right”) (slide 1 of 3)

- The IDDR approach:
 - Involves organizing the issues and approaching them systematically
 - Can help eliminate various alternatives and identify the strengths and weaknesses of the remaining alternatives
 - Contains four steps

Step 1: Inquiry

- The decision makers must identify the ethical problem and all the parties involved—the stakeholders.
- It is important that the decision makers not frame the issue in a way that gives them the answer they might prefer.

3-4a A Systematic Approach: IDDR (“I Desire to Do Right”) (slide 2 of 3)

Step 2: Discussion

- Once the ethical problem(s) have been clarified, a list of possible actions can be compiled.
- In discussing these alternatives, decision makers should:
 - Take time to think through each alternative completely
 - Analyze each alternative’s potential impact on stakeholders
 - Evaluate each option’s:
 - Strengths
 - Weaknesses
 - Ethical consequences
 - Legal consequences
- At this point, decision makers should consider what they should do before considering what they can or will do.

3-4a A Systematic Approach: IDDR (“I Desire to Do Right”) (slide 3 of 3)

Step 3: Decision

- With all the relevant facts collected and the alternatives thoroughly analyzed and discussed, the decision makers should craft a consensus decision or plan of action.
- Once the decision has been made, the decision makers should articulate the reasons they arrived at the decision so they can share with stakeholders why the course of action is an ethical solution to the problem.

Step 4: Review

- After the decision is implemented, the decision makers should review the effectiveness of the solution.

3-5 Business Ethics on a Global Level

- Individual countries and regions have different ethical expectations and priorities.
 - Some of these differences are based on religious values, whereas others are cultural in nature.
 - Such differences can make it even more difficult to determine what is ethical in a particular situation.

3-5a World Religions, Cultural Norms, and Ethics

- Global businesses need to be conscious of the impact of different religious principles and cultural norms on ethics.
 - **Example:** It would be considered unethical for a U.S. business to produce alcohol in a country where it is forbidden for religious reasons.

3-5b Outsourcing

- **Outsourcing** – The practice by which a company hires an outside firm or individual to perform work rather than hiring employees.
- Ethical problems involving outsourcing most often arise when global companies outsource work to other countries in an attempt to save on labor costs.
- Outsourcing covers a wide spectrum of ethical gray areas and is not always clearly unethical.
 - **Example:** Outsourcing domestically (such as when companies hire outside firms to transport goods) generally does not raise ethical issues.

3-5c Avoiding Corruption

- The Foreign Corrupt Practices Act prohibits U.S. businesses from making payments to (bribing) foreign officials to secure beneficial contracts, with certain exceptions.
 - Payments are permissible:
 - If they are lawful within the foreign country
 - For small amounts to minor officials to facilitate or speed up the performance of administrative services
 - To private foreign companies or other third parties
- Corruption is widespread in some nations, and it can be the norm in dealing with both government and businesses in certain locations.
 - Thus, global companies must take special care when doing business in countries where corruption is common.

3-5d Monitoring the Employment Practices of Foreign Suppliers

Wages and Working Conditions

- U.S. businesses may hire contractors in developing nations that engage in unethical behavior at their worksites.
 - **Examples:** Hiring women and children at below-minimum-wage rates or requiring employees to work long hours in a workplace full of health hazards

Corporate Watch Groups

- A company's actions in other nations can be discovered and publicized by “corporate watch” groups.
 - As a result, U.S. businesses usually take steps to avoid such adverse publicity—either by refusing to deal with certain suppliers or by arranging to monitor their suppliers' workplaces to make sure that employees are not being mistreated.

Appendix

Note to Instructor:

The following activities are also included at the end of each chapter.
We have provided them here to aid with in-class facilitation.

Practice and Review: Ethics in Business

- James Stilton is the chief executive officer (CEO) of RightLiving, Inc., a company that buys life insurance policies at a discount from terminally ill persons and sells the policies to investors.
- RightLiving pays the terminally ill patients a percentage of the future death benefit (usually 65 percent) and then sells the policies to investors for 85 percent of the value of the future benefit.
- The patients receive the cash to use for medical and other expenses.
- The investors are “guaranteed” a positive return on their investment, and RightLiving profits on the difference between the purchase and sale prices.
- Stilton is aware that some sick patients might obtain insurance policies through fraud (by not revealing the illness on the insurance application).
- Insurance companies that discover this will cancel the policy and refuse to pay.
- Stilton believes that most of the policies he has purchased are legitimate, but he knows that some probably are not.

Using the information presented in the chapter, answer the following questions.

Practice and Review: Questions (slide 1 of 4)

1. Would a person who adheres to the principle of rights consider it ethical for Stilton not to disclose the potential risk of cancellation to investors? Why or why not?

Practice and Review: Questions (slide 2 of 4)

2. Using Immanuel Kant's categorical imperative, are the actions of RightLiving, Inc., ethical? Why or why not?

Practice and Review: Questions (slide 3 of 4)

3. Under utilitarianism, are Stilton's actions ethical? Why or why not? If most of the policies are, in fact, legitimate, does this make a difference in your analysis?

Practice and Review: Questions (slide 4 of 4)

4. Using the IDDR approach, discuss the decision process Stilton should use in deciding whether to disclose the risk of fraudulent policies to potential investors.

Debate This...

Executives in large corporations are ultimately rewarded if their companies do well, particularly as evidenced by rising stock prices. Consequently, should we let those who run corporations decide what level of negative side effects of their goods or services is “acceptable”?