

## **Chapter 2– The Ethical Basis of Law and Business Management**

Business owners and managers traditionally have had to ensure that their profit-making activities did not exceed the ethical boundaries established by society. In the past, these boundaries were often regarded as being the same as the limits of the law—that is, if something was legal, it was ethical.

The tough question is:

### The Nature of Business Ethics

Ethics—is the study of what constitutes right or wrong behavior. It is the branch of philosophy that focuses on morality and the way in which moral principles are applied to daily life. Ethics has to do with questions relating to the fairness, justness, rightness, or wrongness of an action.

Although the terms ethical and moral are often used interchangeably, the terms refer to slightly different concepts.

Business ethics—

Many of our ethical decisions are made for us—by our laws. However, simply obeying the law does not fulfill all ethical obligations. Some actions in business may be legal but not ethical.

### Sources of Ethical Standards

Ethical reasoning relating to business traditionally has been characterized by two fundamental approaches. One approach defines ethical behavior in terms of duty or formalism (deontology). Formalism or duty-based ethical standards are often derived from moral principles rooted in religious sources. In the Judeo-Christian tradition, the Ten Commandments establish rules for moral action. Other religions have their own sources of revealed truth—such as the Koran in the Muslim world. Within the confines of their influence, moral principles are universal and absolute—they are not to be questioned.

When an act is prohibited by religious teachings that serve as the foundation of a person's moral or ethical standards, the act is unethical for that person and should not be undertaken, regardless of the consequences.

Ethical standards based on a concept of duty may also be derived solely from philosophical principles.

The social contract theory of John Rawls furnishes an important recent example of how formalism has influenced thinking about business and personal ethics. Social contract theory concerns itself with how to construct a just society given the many inequalities of wealth, knowledge, and social status. Rawls suggests a simple first step in determining the ethical values on which a just society can be built. We should assume that we do not know our age, gender, race, intelligence, strength, wealth, or social status.

Rawls proposes two ethical principles. First, everyone is entitled to certain equal basic rights, including liberty, freedom of association, and personal security. Second, although there may be social and economic inequalities, these inequalities must be based on what a person does, not on who a person is, and everyone must have an equal opportunity for achievement.

A second approach is outcome-based ethics or consequentialism. This approach concerns itself with the moral consequences of actions rather than with the morality of the actions themselves. For the consequentialist, lying itself is not unethical. It is the consequences of lying that must be evaluated for their ethical implications.

The dominant form of outcome-based ethics is utilitarianism.

Utilitarianism—

## Obstacles to Ethical Business Behavior

Some business persons knowingly engage in unethical behavior because they think that they can get away with it. Examples of this kind of unethical behavior include

In other situations, business persons who would choose to act ethically may be deterred from doing so because of situational circumstances or external pressures.

### Ethics and the Corporate Environment

Some contend that the nature of the corporate structure itself acts as a deterrent to ethically responsible behavior.

The corporate setting complicates ethical decision-making because no one person makes a corporate decision. To some extent the corporate collectivity may shield corporate personnel from both personal exposure to the consequences of their actions and personal accountability for those decisions. For example, suppose that a corporate board decides to market a new product that results in several consumers' deaths. Those who made the decision do not witness or deal directly with the consequences.

Much unethical behavior occurs simply because it is not always clear what ethical standards and behaviors are appropriate or acceptable in a given context.

Another deterrent to ethical behavior exists when corporate management, by its own conduct, indicates that ethical considerations take second place.

## Corporate Social Responsibility

We now consider this question: How can business persons act in an ethically responsible manner and at the same time make profits for their firms or their firms' owners? This question is at the heart of the debate surrounding the concept of corporate social responsibility. The question of corporate social responsibility concerns the extent to which a corporation has ethical duties to various groups in society that go beyond its legally prescribed duties.

### Duty to Shareholders

Corporate directors and officers have a duty to act in the shareholders' interest. Traditionally, it was perceived that this duty to shareholders took precedence over all other corporate duties and that the primary goal of corporations should be profit maximization.

### Duty to Employees

One of the primary concerns of every employer is the ability to control the workplace environment. Federal laws require employers to offer equal opportunities to all job applicants and employees. Does an employer also have ethical obligations to employees that go beyond these legal duties?

One conflict of duties that sometimes faces employers poses the choice of being sued for sexual harassment against the choice of being sued for wrongful discharge. Suppose that an employee of a company complains to her supervisor that a co-worker is sexually harassing her. The company immediately investigates the claim, and on finding that it is substantiated, promptly fires the harassing employee. The employee then sues the firm for wrongful discharge.

### Duty to Consumers

Clearly, a corporation has a duty to the users of its products. This is not just an ethical duty but a legal one as well.

Suppose an American firm learns that one of its products—glue—is being inhaled by some children in several Latin American countries. What is the firm's responsibility in this situation?

Whenever a corporation markets a product, the law imposes a duty on the firm to warn consumers, among other things, of the harms that can result from foreseeable misuses. When a risk is open and obvious, the courts tend to hold that no warning is necessary.

### Duty to the Community

In some circumstances, the community in which a business enterprise is located has a substantial stake in the firm. If the company decides that it would be profitable to close the plant or move it to another location, the employees and the community would suffer as a result.

### Duty to Society

Perhaps the most disputed area in the controversy surrounding corporate social responsibility is the nature of a corporation's duty to society at large. Those who contend that corporations should first and foremost attend to the goal of profit maximization would argue that it is by generating profits that a firm can best contribute to society. Because our society values wealth as an ethical goal, corporations, by contributing to wealth, automatically are acting ethically.

Critics of the profit-maximization view believe that corporations should become actively engaged in seeking and furthering solutions to social problems.

### The Corporate Balancing Act

Today's corporate decision makers are, in a sense, poised on a fulcrum between profitability and ethical responsibility. Instead of maximum profits, many firms today aim for optimum profits—profits that can be realized while staying within legal and ethical limits.

### Measuring Corporate Social Responsibility

## Corporate Philanthropy

Corporations have generally contributed some of their shareholders' wealth to meet social needs. Frequently, corporations establish separate nonprofit foundations for this purpose.

## Corporate Process

Corporations are being judged less on the basis of their philanthropy than on their practices, or corporate process. Corporate process refers to

## It Pays To Be Ethical

Most corporations today have learned that it pays to be ethically responsible—even if it means less profits in the short run. If a corporation fails to conduct its operations ethically or respond quickly to an ethical crisis, its goodwill and reputation will likely suffer as a result. Also, companies that demonstrate a commitment to ethical behavior often receive more lenient treatment from government agencies or the courts.

## Ethics in the Global Context

Given the varied cultures and religions of the world's nations, one might expect frequent conflicts in ethics between foreign and US business persons. In fact, many of the most important ethical precepts are common to virtually all nations. Some important ethical differences do exist.

Another ethical problem in international business dealings has to do with the legitimacy of certain side payments to government officials. In the US, the majority of contracts are formed within the private sector. In many foreign countries, decisions on most major construction and manufacturing contracts are made by government officials because of extensive government regulation and control over trade. Side payments to government officials in exchange for favorable business contracts are not unusual nor are they considered to be unethical.