CHAPTER 9

Strategy, Ethics, and Social Responsibility

Corporations are economic entities, to be sure, but they are also social institutions that must justify their existence by their overall contribution to society.
—Henry Mintzberg, Robert Simons, and Kunal Basu, professors

Social obligation is much bigger than supporting worthy causes. It includes anything that impacts people and the quality of their lives.
—William Ford, Jr., Chairman of Ford Motor Company

There is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say engages in free and open competition, without deception or fraud.
—Milton Friedman, Nobel Prize–winning economist

It takes many good deeds to build a good reputation and only one bad one to lose it.
—Benjamin Franklin

But I'd shut my eyes in the sentry box so I didn't see nothing wrong.
—Rudyard Kipling

Clearly, in capitalistic or market economies, top-level managers of privately owned companies are responsible and accountable for operating the enterprise profitably and acting in shareholders' best interests; management's fiduciary duty to operate the enterprise in a manner that creates value for shareholders is not a matter for serious debate. Just as clearly, a company and its personnel are duty-bound to obey the law and comply with governmental regulations. But does a company also have a duty to go beyond legal requirements and hold all company personnel responsible for conforming to high ethical standards? Does a company have an obligation to be a good corporate citizen? Should a company display a social conscience by devoting a portion of its resources to improving the quality of life in the communities where it operates and in society at large? How far should a company go in protecting the environment, conserving natural resources for use by future generations, and ensuring its operations do not ultimately endanger the planet?

This chapter focuses on whether a company, in the course of trying to craft and execute a strategy that delivers value to both customers and shareholders, also has a duty to (1) act in an ethical manner, (2) be a committed corporate citizen and allocate some of its financial and human resources to improving the well-being of employees, the communities in which it operates, and society as a whole, and (3) screen its strategic initiatives and operating practices for possible negative effects on the environment and future generations of the world's population.

What Do We Mean by Business Ethics?

Ethics concerns the principles and standards of right and wrong conduct. **Business ethics** concerns the application of ethical principles and standards to the actions and decisions of business organizations and the conduct of their personnel.[1] *Ethical principles in business are not materially different from ethical principles in general.* Why? Because business actions must be judged in the context of society's standards of what is ethically right and wrong, not by a special set of rules that apply just to business conduct. If dishonesty is considered unethical and immoral, then dishonest behavior in business—whether it relates to customers, suppliers, employees or shareholders—qualifies as equally unethical and immoral. If being ethical entails not deliberately harming others, then businesses are ethically obligated to recall a defective or unsafe product, regardless of the cost. If society deems bribery unethical, then it is unethical for company personnel to make payoffs to government officials to win government contracts or bestow gifts and other favors on prospective customers to win or retain their business.

Where Do Ethical Standards Come From?

Notions of right and wrong, fair and unfair, moral and immoral, ethical and unethical are present in all societies and cultures. But there are three distinct schools of thought about the extent to which ethical standards travel across cultures and whether multinational companies can apply the same set of ethical standards in any and all locations where they operate.

The School of Ethical Universalism

According to the school of **ethical universalism,** the most fundamental concepts of what is right and what is wrong are *universal* and transcend most all cultures, societies, and religions.[2] For instance, being truthful (or not lying or not being deliberately deceitful) strikes a chord of what's right in the people of all nations. Likewise, demonstrating integrity of character, not cheating, and treating people with courtesy and respect are concepts that resonate across countries, cultures, and religions. In most societies, people would concur it is unethical to knowingly expose workers to toxic chemicals and hazardous materials or to sell products known to be unsafe or harmful to the users or to pillage or degrade the environment. These universal ethical traits and behaviors are considered virtuous and represent standards of conduct that a good person is supposed to believe in and to observe. Thus, adherents of the school of ethical universalism maintain *it is entirely appropriate to expect all members of society (including all personnel of all companies worldwide) to conform to universal ethical standards*.[3]

CORE CONCEPT

According to the school of **ethical universalism**, common moral agreement about right and wrong actions and behaviors across multiple cultures and countries gives rise to universal ethical standards that apply to the members of all societies, all companies, and all business people.

The strength of ethical universalism is that it draws upon the collective views of multiple societies and cultures to put some clear boundaries on what constitutes ethical and unethical business behavior no matter what country or culture a company or its personnel are operating in. This means in those instances where basic moral standards do not vary significantly according to local cultural beliefs, traditions, religious convictions, or time and circumstance, a multinational company can develop a single code of ethics and apply it more or less evenly across its worldwide operations.[4] It can avoid the slippery slope that comes from having different ethical standards for different company personnel depending on where in the world they are working.

The School of Ethical Relativism

According to the school of **ethical relativism,** while there are a few universal moral prescriptions—like being truthful and trustworthy—that apply in most every society and business circumstance, there are meaningful variations in what societies generally agree to be ethically right and wrong in the conduct of business activities. Indeed, differing religious beliefs, historic traditions and customs, core values and beliefs, and behavioral norms across countries and cultures frequently give rise to different standards about what is fair or unfair, moral or immoral, and ethically right or wrong. For instance, European and American managers often establish standards of business conduct and ethical behavior that protect such core human rights as freedom of movement and residence, freedom of speech and political opinion, fairness of treatment, equal protection under the law, and the right to privacy. In China, where societal commitment to basic human rights is weak, human rights considerations play a small role in determining what is ethically right or wrong in conducting business activities. In Japan, managers believe showing respect for the collective good of society is an important ethical consideration. In Muslim countries, managers typically apply ethical standards compatible with the teachings of Mohammed. Consequently, the school of ethical relativism holds that a "one-size-fits-all" template for judging the ethical appropriateness of business actions and the behaviors of company personnel is totally inappropriate. Rather, the underlying thesis of ethical relativism is that whether certain actions or behaviors are ethically right or wrong depends on what a local country or culture decides is ethically right or wrong—in other words, when there are cross-country or cross-cultural differences in ethical standards, it is appropriate for *local ethical standards to take precedence over ethical standards elsewhere.*[5] This need to contour local ethical standards to fit local customs, local notions of fair and proper individual treatment, and local business practices gives rise to multiple sets of ethical standards. In a world of ethical relativism, there are few absolutes when it comes to business ethics, and thus few ethical absolutes for consistently judging the ethical correctness of a company's conduct in various countries and markets.

CORE CONCEPT

According to the school of **ethical relativism**, differing religious beliefs, historic traditions and customs, core values and beliefs, and behavioral norms across countries and cultures give rise to *multiple sets of standards concerning what is ethically right or wrong.* These differing standards mean that whether certain business-related actions or behaviors are ethically right or wrong depends on the prevailing local ethical standards.

While the ethical relativism rule of "When in Rome, do as the Romans do" appears reasonable, it leads to the conclusion that what prevails as local morality is an adequate and definitive guide to ethical behavior. But this poses some challenging ethical dilemmas. Consider the following two examples.

The Use of Underage Labor In industrialized nations, the use of "underage" workers is considered taboo. Social activists are adamant that child labor is unethical, that legislation mandating compulsory education is needed in all countries across the world, and that companies should neither employ children under the age of 18 as full-time employees nor source any products from foreign suppliers that employ underage workers. Many countries have passed legislation forbidding the use of underage labor or, at a minimum, regulating the employment of workers under the age of 18. However, in Ethiopia, Zimbabwe, Pakistan, Afghanistan, Somalia, Burma, North Korea, Yemen, Bangladesh, Botswana, Sri Lanka, Ghana, Nigeria, Sudan, and 45 other countries, where poverty rates are very high, children are typically viewed as potential, even necessary, workers.[6] In other countries, like India, China, Russia, and Brazil, child labor laws are poorly enforced.[7] A 2013 report issued by the International Labor Organization estimated that as of 2012 there were about 168 million child laborers age 5 to 17 and that some 85 million of these were engaged in hazardous work.[8]

While exposing children to hazardous work, forced labor, and long work hours is unquestionably deplorable, the fact remains that poverty-stricken families in many poor countries cannot subsist without the work efforts of young family members; sending their children to school instead of having them participate in the workforce is not a realistic option. Hence, greatly restricting the permissible kinds of employment of children in poor countries (especially those in the 12–17 age group)—owing to strong pressures from

Strict adherence to the principles of ethical relativism leads to the untenable conclusion that child labor is ethically impermissible in countries where it is contrary to local custom, but it is ethically permissible in countries where the use of child labor is common practice.

well-meaning activist groups and government organizations whose systems of values and beliefs prompt them to work toward banning many forms of child labor—risks the unintended consequences of forcing children in impoverished families to seek work in "hidden" parts of the economy of their countries or be out on the street begging or even reduced to trafficking in drugs or engaging in prostitution.[9] To the extent that such unintended consequences occur, have the best interests of underage workers, impoverished families, and society in general been well served? On the other hand, notwithstanding the principle of ethical relativism, it is logical quicksand to contend that child labor is unethical in industrialized countries (because it is contrary to local custom) yet is ethically permissible in impoverished countries where child labor is common practice. It would seem ethically inconsistent to declare the employment of underage labor to be an unethical business practice in one locality and an ethical business practice in another location simply because of differing local customs.

The Payment of Bribes and Kickbacks A particularly thorny area facing multinational companies is the degree of cross-country variability in paying bribes.[10] In many countries, it is common for companies to pay bribes to government officials to win a government contract, obtain a license or permit, or facilitate an administrative ruling. In some developing nations, it is difficult for any foreign or domestic company to move goods through customs without paying off low-level officials.[11] Senior managers in China and Russia often use their power to obtain kickbacks when they purchase materials or other products for their companies.[12] Likewise, in many countries it is normal to make payments to prospective customers to win or retain their business. Some people stretch to justify the payment of bribes and kickbacks on grounds that bribing government officials to get goods through customs or giving kickbacks to customers to retain their business or win new orders is simply a payment for services rendered, in the same way that people tip for service at restaurants.[13] But while this argument is a clever and pragmatic way to rationalize viewing bribes as a normal and maybe unavoidable cost of doing business, it rests on moral quicksand.

Companies that forbid the payment of bribes and kickbacks in their codes of ethical conduct and that are serious about enforcing this prohibition face a particularly vexing problem in those countries where bribery and kickback payments are an entrenched local custom and are not considered unethical.[14] Refusing to pay bribes or kickbacks in these countries (to comply with the company's code of ethical conduct) is often tantamount to losing business to competitors willing to make such payments—an outcome that penalizes ethical companies and ethical company personnel (who may suffer lost sales commissions or bonuses). But, on the other hand, blinking an eye at a company's code of ethical conduct and going along with the payment of bribes or kickbacks not only undercuts enforcement of and adherence to the company's code of ethics but can also risk breaking the law. The Foreign Corrupt Practices Act (FCPA) prohibits U.S. companies from paying bribes to government officials, political parties, political candidates, or others in all countries where they do business. The Organization for Economic Cooperation and Development (OECD) has anti-bribery standards that criminalize the bribery of foreign public officials in international business transactions—all 34 OECD member countries and 6 nonmember countries have adopted these standards.[15]

Despite laws forbidding bribery to secure sales and contracts, the practice persists. Siemens, one of the world's largest corporations and headquartered in Munich, Germany, was fined $1.6 billion by the U.S. and German governments for paying more than $800 million to more than 4,000 well-placed government officials in Asia, Africa, Europe, the Middle East, and Latin America between 2001 and 2007 to help secure huge public works contracts; moreover, there was evidence that bribery of public officials was a core element of Siemens' strategy. Hewlett-Packard paid $16.25 million to settle allegations that it bribed Texas school officials with expensive gifts in exchange for federally funded contracts that paid for Internet connections for schools and libraries. Daimler AG, the maker of Mercedes-Benz vehicles, paid $185 million in fines to settle charges that it used secret bank accounts to make 200 illicit payments totaling more than $56 million to foreign officials in 22 countries between 1998 and 2008. In 2014, Alcoa agreed to pay $384 million to settle charges that it used bribes to lock in lucrative contracts in Bahrain. In 2013, the Ralph Lauren Corporation agreed to forfeit illicit profits made due to bribes paid by a subsidiary in Argentina. An OECD study of 427 criminal proceedings for bribery in 41 European countries during the period February 1999-June 2014 revealed that fines totaling nearly $5 billion were imposed on 261 individuals and companies, with prison sentences for 80 individuals and suspended prison sentences for an additional 38 individuals; most of the cases involved bribery of public officials and were undertaken through intermediaries with the knowledge of senior management.[16]

Using the Principle of Ethical Relativism to Create Ethical Standards Is Problematic for Multinational Companies Relying upon the principle of ethical relativism to determine what is ethically right or wrong poses major problems for multinational companies wanting to address the real issue of what ethical standards to enforce companywide. It is a slippery slope indeed to resolve conflicting ethical standards for operating in different countries. How can a multinational company, standing on the principle of ethical relativism, declare it ethically permissible for company personnel to pay bribes and kickbacks in countries where such payments are customary but ethically impermissible to make such payments in those countries where bribes and kickbacks are either not customary or illegal?

Business leaders who rely upon the principle of ethical relativism to justify conflicting ethical standards for operating in different countries have little moral basis for establishing or enforcing ethical standards companywide. Rather, when a company's ethical standards vary from country to country, the clear message being sent to employees is that the company has no ethical standards or convictions of its own and prefers to let its standards of ethically right and wrong be governed by the customs and practices of the countries in which it operates. *Applying multiple sets of ethical standards without a higher-order moral compass is scarcely a basis for holding company personnel to high standards of ethical behavior.*

> Managers in multinational enterprises have to figure out how to navigate the gray zone that arises when their company operates in two or more countries or cultures with differing customs and ethical standards. Having multiple standards that vary by locale is equivalent to having no standard.

Ethics and Integrative Social Contracts Theory

Integrative social contracts theory provides yet a middle position between the opposing views of universalism (that the same set of ethical standards should apply everywhere) and relativism (that ethical standards should be governed by local custom and practice).[17] According to this theory, the ethical standards a company should try to uphold are governed both by (1) a limited number of universal ethical principles widely recognized as putting legitimate ethical boundaries on actions and behavior in *all* situations and (2) the circumstances of local cultures, traditions, and shared values that further prescribe what constitutes ethically permissible behavior and what does not. However, *universal ethical norms always take precedence over local ethical norms.* In other words, universal ethical principles apply in those situations where most all societies—endowed with rationality and moral knowledge—have common moral agreement on what actions and behaviors fall inside the boundaries of what is right and which ones fall outside. *These mostly uniform and universal agreements about what is morally right and wrong form a "social contract" or contract with society that is binding on all individuals, groups, organizations, and businesses in terms of establishing right and wrong and drawing the line between ethical and unethical behaviors.*

> **CORE CONCEPT**
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> According to **integrated social contracts theory**, universal ethical principles or norms based on the collective views of multiple cultures and societies combine to form a "social contract" that all individuals, groups, organizations, and businesses in all situations have a duty to observe. So long as the boundaries of this social contract are observed, there is legitimate room for local cultures or groups to prescribe what other actions may or may not be ethically permissible. However, according to integrated social contracts theory, *adherence to universal or "first-order" ethical norms must always take precedence over local or "second-order" norms.*

But these universal ethical principles or norms nonetheless still leave some "moral free space" for the people in a particular country (or local culture or even a company) to make specific interpretations of what other actions may or may not be permissible within the bounds defined by universal ethical principles. Hence, while firms, industries, professional associations, and other business-relevant groups are "contractually obligated" to society to observe universal ethical norms, they have the discretion to go beyond these universal norms and specify other behaviors that are out of bounds and place further limitations on what is considered ethical. Both the legal and medical professions have standards regarding what kinds of advertising are ethically permissible and what kinds are not. Food products companies are beginning to establish ethical guidelines for judging what is and is not appropriate advertising for inherently unhealthy food products that may cause dietary or obesity problems for people who eat them regularly or consume them in large quantities.

The strength of integrated social contracts theory is that it accommodates the best parts of ethical universalism and ethical relativism. It is indisputable that cultural differences impact how business is conducted in various parts of the world and that these cultural differences sometimes give rise to different ethical norms. But it is just as indisputable that *some ethical norms are more authentic or universally applicable than others, meaning that in many instances of cross-country differences one side may be more "ethically correct" or "more right" than another.* In such instances, resolving cross-cultural differences in what is ethically permissible versus what is not entails applying universal or "first-order" ethical norms and overriding the local or "second-order" ethical norms. A good example of the application of integrated social contracts theory is the payment of bribes and kickbacks. Yes, bribes and kickbacks are common in some countries, but does this justify paying them? *Just because bribery flourishes in a country does not mean it is an authentic or legitimate ethical norm.* Virtually all of the world's major religions (Buddhism, Christianity, Confucianism, Hinduism, Islam, Judaism, Sikhism, and Taoism) and all moral schools of thought condemn bribery and corruption.[18] Therefore, a multinational company might reasonably conclude that there is a universal ethical principle to be observed here—one of refusing to condone bribery and kickbacks on the part of company personnel no matter what the local custom is and no matter what the sales consequences are.

The Principles of Integrated Social Contracts Theory Work Well for Multinational Companies

Integrated social contracts theory offers clear guidance for the managers of multinational companies in resolving cross-country ethical differences: Those parts of the company's code of ethics that involve universal ethical norms must be enforced worldwide, but within these boundaries there is room for company personnel to engage in behaviors that conform to local ethical standards. Allowing room for the observance of local or second-order ethical norms is a pragmatic and defensible middle-ground—it means a multinational enterprise does not have to adopt the role of standard-bearer of moral truth and impose inflexible ethics standards worldwide no matter what. And it avoids the fatal weakness of using the principle of ethical relativism to set ethical standards of right and wrong that are totally governed by the customs and practices of the countries in which it operates and thus give company personnel a license to engage in behavior that clearly violate universal ethical norms.

The Three Categories of Management Morality

Three categories of managers stand out with regard to ethical and moral principles in business affairs:[19]

- *The moral manager.* Moral managers are dedicated to high standards of ethical behavior, both in their own actions and in their expectations of how the company's business is to be conducted. They see themselves as stewards of ethical behavior and believe it is important to pursue success in business within the confines of both the letter and the spirit of what is ethical and legal. They typically regard complying with the law as an ethical minimum, and they operate well above what the law requires.

- *The immoral manager.* Immoral managers have no regard for so-called ethical standards in business and pay no attention to ethical principles in making decisions and conducting the company's business. Their philosophy is that good businesspeople cannot spend time watching out for the interests of others and agonizing over "the right thing to do" from an ethical perspective. In the minds of immoral managers, nice guys come in second and the competitive nature of business requires that you either trample on others or get trampled yourself. They believe what really matters is the single-minded pursuit of their own best interests. They are living examples of capitalistic greed, caring only about their own or their organization's gains and successes. Immoral managers may even be willing to short-circuit legal and regulatory requirements if they think they can escape detection. And they are always on the lookout for legal loopholes and creative ways to get around rules and regulations that block or constrain actions they deem in their own or their company's self-interest. Immoral managers are thus the bad guys. They have few scruples, little or no integrity, and are willing to do most anything they believe they can get away with. It doesn't bother them much to be seen by others as wearing the black hats.

- *The amoral manager.* Amoral managers believe businesses ought to be able to do whatever the prevailing laws and regulations allow them to do. If particular business actions and behaviors are legal and do not violate prevailing government regulations, they should not be seen as unethical. Amoral managers view the observance of high ethical standards (doing more than what laws and regulations require) as too Sunday-schoolish for the tough competitive world of business, even though observing some higher ethical considerations may be appropriate in life outside of business. Their concept of right and wrong tends to be lawyer driven—"How much can we get by with?" and "What are the risks of going ahead even if a particular action is borderline?"

CORE CONCEPT

Amoral managers believe that businesses ought to be able to do whatever current laws and regulations allow them to do without being shackled by any ethical considerations. They think that what is permissible and what is not are governed entirely by prevailing laws and regulations, not by societal concepts of right and wrong.

By some accounts, the population of managers is said to be distributed among all three types in a bell-shaped curve, with immoral managers and moral managers occupying the two tails of the curve, and amoral managers occupying the broad middle ground.[20] Furthermore, within the population of managers, there is experiential evidence to support that while the average manager is amoral most of the time, he or she may slip into a moral or immoral mode on occasion, based on a variety of impinging factors and circumstances.

Evidence of Managerial Immorality in the Global Business Community

There is considerable evidence that a sizable majority of managers are either amoral or immoral. Ongoing research by Berlin-based Transparency International shows corruption among public officials and in business transactions is widespread across the world.[21] Table 9.1 shows some of the countries where public corruption is believed to be lowest and highest. A global community where corruption is so prevalent suggests that all too few companies ground their strategies on exemplary ethical principles or insist that company personnel measure up to high ethical standards. And, as many business school professors have noted, there are considerable numbers of amoral business students in our classrooms. So the task of rooting out shady and corrupt business practices and creating an ethically strong global business climate is certain to be arduous and time-consuming.

Table 9.1 Corruption Perceptions Index, Selected Countries, 2012-2014

(The CPI scores are based on a 100-point scale, where 100 = very clean and 0 = highly corrupt)

Country	2014 CPI Score	Country	2014 CPI Score	Country	2014 CPI Score
Denmark	92	United States	74	South Africa	44
New Zealand	91	Chile	73	Brazil	43
Finland	89	Uruguay	73	Greece	43
Sweden	87	France	69	Italy	43
Norway	86	Portugal	63	India	38
Switzerland	86	Puerto Rico	63	China	36
Singapore	84	Poland	61	Mexico	35
Netherlands	83	Taiwan	61	Argentina	34
Canada	81	Israel	60	Russia	28
Australia	80	Spain	60	Pakistan	27
Germany	79	South Korea	55	Iran	27
United Kingdom	78	Malaysia	52	Syria	20
Japan	76	Czech Republic	51	Iraq	16
Hong Kong	74	Saudi Arabia	49	Afghanistan	12
Ireland	74	Turkey	45	North Korea	8

Source: Transparency International, *2014 Corruption Perceptions Index*, http://transparency.org/cpi2014/results (accessed February 19, 2015).