# Chapter Two

## Ethical Principles in Business

### 2.2. Ethical Concepts

Ethics is the branch of philosophy that is used to evaluate human actions. Some basic ethical concepts in business are as follows:

- **Ethical subjectivism**: This concept emphasizes that the ethical choice of the individual decides the rightness or wrongness of his behavior.
- **Ethical relativism**: According to this concept, no principle is universally applicable and so it would be inaccurate to measure the behavior of one society with another's principles or standards. Relativism overlooks the fact that there may be enough evidence to believe that an ethical practice is based on false belief, illogical reasoning, and so on.
- **Consequentialism**: Consequentialism is based on two ideas: the concept of value and the maximization of value. If, for example, honesty is considered a value, an act is considered ethical only if it maximizes this value. An act, which does not maximize the said value, is not ethically permissible.
- **Deontological ethics**: This concept stresses that ethical values can be developed from the concepts of reason as all rational individuals possess the ability to reason. We may, for example, end up causing pain unknowingly while trying to create happiness. Therefore, the ethical value of an action cannot be determined by its consequences. Instead, it is in the motive that lies behind the particular action.
- **Ethics of virtue**: This concept emphasizes those traits that give the individual a sense of satisfaction from ethical point of view. Virtuous acts like courage, honesty, tolerance and generosity are done as a way of living and not by chance.
- **Whistle blowing**: Whistle blowing refers to the attempt of an employee to disclose what he or she believes to be illegal behavior in or by the organization. From one point of view, this seems to deceive the principle of honesty in business ethics, as it is taken for granted that the employees of an organization need to be loyal to its workings. However, when loyalty to one's organization in particular is perceived to be harming one's general loyalty to mankind, the act of whistle blowing is justified. Failure on the part of the management of the organization to fulfill its social obligations calls for whistle blowing. It is the responsibility of the whistle blower to be careful about revealing the organization's secrets and to consider the harm it may cause to his colleagues and shareholders.

### 2.3. **Ethical Models**

Ethical models can be used to define ethical situations and manage ethical dilemmas that may occur in the organizations. The Golden Rule Model and The Right-driven or Kantian model are two operational models that have emerged from the work of philosopher Immanuel Kant.

### The Golden Rule Model

This model—originated from the New Testament—specifies people should treat others in the same manner that they themselves would like to be treated. It is a fundamental principle found in every culture and religion and it is the most important basis for the modern concept of human rights. It is also called the ethics of reciprocity as it stimulates an individual to put oneself in the other person's shoes and then evaluate how one would wish to be treated in that particular situation. This proves that this rule is absurd without identifying the receiver and the situation. The ethics of reciprocity should not be confused with revenge or penalizing justice. The ethics also mentions that one has the freedom to do anything as long as those activities do not harm anyone. If this golden rule is applied to every anomaly, then many unethical consequences may result in causing harm to others and perfectionists may charge others with critical analysis, which may lead to harassments. Different people have different ideologies, beliefs and may belong to different cultural heritages. This difference is the reason behind the difference people's behavior towards various situations.

### The Kantian Model

This model is based on the hypothesis that everybody has some fundamental rights in this ethical universe. So any action is ethically correct if it reduces the stakeholders' collective violation of rights. This model willingly provides assistance in the internal audit review and helps in managerial decision-making. Kant did not believe that any outcome was good from its origin. According to him good is not always intrinsic. He did not believe in 'good' character traits like ingenuity, intelligence and courage. In fact, he used the term 'good' to describe 'goodwill', by which he meant the resolve to perform the act purely in accordance with one's duty.

If the actions are predetermined then they cannot be described as free and moral. He believed that to act morally, freedom is required. According to Kant there are two concepts of duty. According to one concept, duty is just following orders imposed by others. The other concept is that duty is internal and can be imposed on oneself. He considered that inclinations constitute motivation whereas others believed that it was the physical world that acted as motivation. But Kant believed that the sources of the physical world might be unreliable, passive and phenomenal. Sometimes, man's mind is over-clouded by sorrows due to his lack of sympathy from others but he still has the power to help those in distress. He no longer needs any support as he is sufficiently occupied with his own inclinations, making him indifferent to the sufferings of others. He becomes adaptive to his sufferings with the help of the patience and endurance he has developed in due course of time. This begins to show his worth of character and temperament.

Most of us live by rules most of the time. Some of them are called categorical imperatives that are unconditional commands which bind everyone at all times. There are two types of imperatives: hypothetical imperative, which is to say that if one wants to achieve success then he should work in a freeway and not bind himself to his inclinations; and categorical imperative, for example, the imperative to always tell the truth as it is unconditional and can be applied at all times.

Kant also introduced maxims, which are subjective rules that guide actions and help an individual to act according to the relevant description. There is sufficient generality in description. All actions have maxims like:

- Never lie to your colleagues.
- Never act in a manner that would make your family or organization ashamed of you.
- Always work hard to be the best performer.

## 2.4**. Ethical Corporate Behavior**

To understand the term ‘organizational ethics’, one has to first try and understand the two terms ‘organization’ and ‘ethics’. An organization is a collection of individuals with a common mission while ‘ethics’ may be described as an attempt or endeavor by individuals, to understand what is ‘right’ or ‘wrong’. Ethics is concerned with the critical analysis of situations. Organizational design and follow a set of core principle or concepts in that attempt to develop ethical corporate behavior.

Organizational ethics is used to consider the issues of morality and rationality in organizations. Organizational ethics is completely different from management ethics. Management ethics focuses on the ethical quality of the decisions and actions taken by managers of an organization. Thus, management ethics deals with the individuals in the organization and organizational ethics deals with all the activities of an organization. Therefore, organizational ethics is collective in scope.

Organizational ethical issues can be handled at three levels. These levels are:

- Corporate mission
- Constituency relations
- Policies and practices

***Corporate mission*** refers to the objectives of an organization that are used to define its ethical responsibilities. Corporate mission also reflects the ambitions and expectations of the employees. Employees should be integrated in a good manner to achieve the corporate mission.

***Constituency relations*** define the responsibilities of the elements of an organization. The elements of an organization may be employees, customers, suppliers, shareholders and the general public. These responsibilities must be handled properly to manage the ethical conduct of business.

Organizational ethics can also be used to evaluate the ***policies and practices*** of the organizations. Public commitment to ethical principles can give way to business and administrative practices.

Organizational ethics also depends on the type of the organization. Organizations can be classified by considering their economic and ethical concerns. Organizations can be classified into four types. These are:

**Exploitative**: Organizations with low economic and ethical concerns are called exploitative organizations. These organizations utilize child labour and use rivers for dumping wastes to maximize their profits.

**Manipulative**: Organizations with high economic performance concerns and low ethical concerns are called manipulative organizations. These organizations use tax laws, labour laws and union leaders to maximize profit.

**Holistic**: Organizations with high ethical concerns and low economic concerns are called holistic organizations. These organizations spend their money in social and environmental purposes.

**Balanced**: Balanced organizations have high ethical and economic concerns. These types of organizations gain profit as well as work for social and environmental purposes.

### 2.4.1. Corporate code of Ethics

Corporate ethical codes can be defined as the standards and beliefs of an organization. These standards and beliefs are made by the managers of the organization. These ethical codes can be used to adjust the thinking and attitude of the individuals in the organization. Ethics codes of organizations are different from the rules of ethics. Ethical rules are the requirements according to which an individual acts.

Organizations can handle the issue of ethics by incorporating the code of business conduct in the corporate structure. These business codes can be used to advise, guide and regulate the behaviour of the individuals in organizations. Organizations can translate the human core values into business codes by using some specific guidelines. Many organizations have formulated codes of ethics for their employees. Most of these codes are very different and some are similar.

These formulated codes of ethics can be used as a tool for developing ethical conduct. Some of the ethical codes formulated by organizations are:

- Ethical codes for discipline
- Proper code of dressing
- Avoiding abusive language or actions
- Punctuality
- Legalistic ethical codes
- Always following instructions from superiors
- Performance of fair performance appraisals
- Personal and cultural ethical codes
- Not using official property for personal use
- Performance of good quality of work
- Having initiative
- Conservation of resources and protection of quality of environment

**Advantages of a Code of Ethics**

Some of the advantages of a code of ethics are:

- Code of ethics can be used to handle outside pressure.
- They can also be used in making overall strategic decisions.

- These codes can be used to define and implement the policies of the organization and distribute work between the employees.
- Code of ethics can be used to optimize the public image and confidence of the organization.
- They can be used to increase the skills and knowledge of the individuals.
- Code of ethics can also be used to respond to the different issues of stakeholders.
- These codes of ethics can be used to discourage improper requests from employees.
- They can also strengthen the enterprise system.

Code of ethics exists in two types

- Principle based statements
- Policy based statements

***Principle based***: designed to affect corporate culture. It defines fundamental values and contains general language about company responsibilities, quality of product and treatment of employees.

***Policy based:*** outline the procedures to be used in specific ethical situations. Example marketing practice, conflict of interest

**2.5. Ethical principles**

The following principles relate to all professionals and must be strictly followed while providing professional service to society:

***Integrity:*** imposes an obligation on all professional accounts to be straight forward and honest in all professional and business relationships. It implies fair dealing and truthfulness. Their work must be uncorrupted by self-interest and not be influenced by the interest of other parties.

***Objectivity:*** imposes an obligation not to compromise their professional or business judgment because of bias, conflict of interest or undue influence of other. A professional accountant shall not perform a professional service if a circumstance or relationship biases or influences the accountants' professional judgment with respect to that service.

***Professional competence and due care:*** imposes the following obligations on all professional accountants:

- To maintain professional knowledge and skill at the level required to ensure that clients or employers receive competent professional service
- To act diligently in accordance with applicable technical and professional standards when providing professional service.

***Confidentiality:*** all unpublished information about a clients or employers affair is confidential. Principle of confidentiality imposed an obligation on all professional accountants to refrain from:

a. Disclosing outside the firm information acquired as a result of professional and business relationship without proper and specific authority or unless there is legal or professional right or duty to disclose
b. Using confidential information to their personal advantage or the advantage of their parties.

Disclosure of confidential information is appropriate if; (a) Disclosure is permitted by law and is authorized by the client or employer. Disclosure is required by law if;

- Production of documents or provision of evidence in the course of legal proceedings
- Disclosure to the public authority of infringements of the law

***Professional Behavior:*** imposes on all professionals to comply with relevant laws and regulations and avoid any action that the professional knows or should know may discredit the profession. Professionals should avoid actions that adversely affect the good reputation of the profession. Example; make exaggerated claims; make un-substained comparisons to the work of others.

**2.6. Theories of business ethics**

1. **Stakeholder theory**: theory of organizational management and business ethics that addresses morale and values in managing an organization. It argues there are other parties than shareholders that a company needs to consider in its decisions and actions. It is based on the assertion that maximizing wealth for shareholders fails to maximize wealth for society and all its members.
2. **Social Contract Theory:** social contract theory sees society as a series of social contracts between members of society and society itself. There is a school of thought which sees social responsibility as a contractual obligation the firm owes to society. An integrated social contract theory was developed by Donaldson and Dunfee as a way for managers make ethical decision making, which refers to macrosocial and microsocial contracts. The former refers to the communities and the expectation from the business to provide support to the local community, and the latter refers to a specific form of involvement.
3. **Legitimacy Theory:** Another theory reviewed in the corporate governance literature is legitimacy theory. Legitimacy theory is defined as "a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate with some socially constructed systems of norms, values, beliefs and definitions. Similar to social contract theory, legitimacy theory is based upon the notion that there is a social contract between the society and an organisation. A firm receives permission to operate from the

society and is ultimately accountable to the society for how it operates and what it does, because society provides corporations the authority to own and use natural resources and to hire employees.

Traditionally profit maximization was viewed as a measure of corporate performance. But according to the legitimacy theory, profit is viewed as an all-inclusive measure of organizational legitimacy. The emphasis of legitimacy theory is that an organization must consider the rights of the public at large, not merely the rights of the investors. Failure to comply with societal expectations may result in sanctions being imposed in the form of restrictions on the firm's operations, resources and demand for its products. Much empirical research has used legitimacy theory to study social and environmental reporting, and proposes a relationship between corporate disclosures and community expectations.

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