

Chapter 2: Understanding Business Ethics and Social Responsibility

Chapter Overview

Just because others see something as ethical doesn't mean you will agree. There is not always a yes/no, right/wrong, black/white answer to everything. We all develop a personal code of ethics that we carry over into our jobs. Sometimes we decide what is ethical based on what is acceptable to others—even though the behavior may be unethical.

This chapter presents a discussion of business ethics, the role of a formal code of ethics, as well as business approaches to social responsibility. The chapter also discusses how the concept of social responsibility applies both to environmental issues and to a firm's relationships with customers, employees, and investors, and how issues of social responsibility and ethics affect small business.

Learning Objectives

- 2-1. Explain how individuals develop their personal codes of ethics and why ethics are important in the workplace.
- 2-2. Distinguish social responsibility from ethics, identify organizational stakeholders, and characterize social consciousness today.
- 2-3. Show how the concept of social responsibility applies both to environmental issues and to a firm's relationships with customers, employees, and investors.
- 2-4. Identify four general approaches to social responsibility and note the role of social responsibility in small business.
- 2-5. Explain the role of government in social responsibility in terms of how governments and businesses influence each other.
- 2-6. Discuss how businesses manage social responsibility in terms of both formal and informal dimensions and how organizations can evaluate their social responsibility.

CHAPTER OUTLINE

Learning Objective 2-1

Explain how individuals develop their personal codes of ethics and why ethics are important in the workplace.

Ethics in the Workplace

Ethics are beliefs about wrong and right or bad and good; **ethical behavior** conforms to individual beliefs and social norms about what is right and good. **Business ethics** refers to ethical or unethical behaviors by employees in the context of their jobs.

A. Individual Ethics

Ethics are based on individual beliefs and social concepts; thus, they vary by person, situation, and culture.

1. **The Law, and the Real World.** Societies adopt formal laws that reflect ethical standards; however, real-world situations are sometimes difficult to interpret.
2. **Individual Values and Morals.** Individuals' personal codes of ethics are determined by a combination of factors, beginning in childhood. Over time, peers and experiences that contribute to ethical beliefs and behavior influence individuals.

B. Business and Managerial Ethics

Managerial ethics are the standards of behavior that guide individual managers in their work.

1. **Behavior Toward Employees.** This category covers hiring and firing, wages and working conditions, and privacy and respect.
2. **Behavior Toward the Organization.** Conflict of interest, confidentiality, and honesty are ethical issues. A **conflict of interest** occurs when an activity may benefit the individual to the detriment of the organization. Many organizations have policies that forbid buyers and other personnel from accepting gifts from suppliers or customers, thus avoiding even the appearance of bribery. Padding expense accounts, and taking office supplies for personal use are examples of problems in the honesty area.
3. **Behavior Toward Other Economic Agents.** Ethics also comes into play in the relationship between the firm and a number of primary agents of interests, such as customers, suppliers, competitors, stockholders, dealers, and unions. In 2009, Bernard Madoff's Ponzi scheme (investment scam) cost hundreds of clients their life savings as he led them to believe that their investments were safe. Cultural norms may indicate that behavior in one country is ethical, while in another country it is unethical. As an example, bribes may be a normal part of doing business in some countries, but illegal in other

countries.

C. Assessing Ethical Behavior

1. A simple process that is often recommended when making ethical decisions is for the person to (1) gather relevant factual information, (2) analyze the facts to determine the most appropriate moral values, and (3) make an ethical decision based on the rightness or wrongness of the proposed activity or policy. Although ethical judgments are not always easy to make or even always agreed upon, this process does at least give a good starting point for an ethical decision making process.

Ethical *norms* include:

1. **Utility:** Does a particular act optimize the benefits to those who are affected by it?
2. **Rights:** Does it respect the rights of all individuals involved?
3. **Justice:** Is it consistent with what's fair?
4. **Caring:** Is it consistent with people's responsibilities to each other?

D. Company Practices and Business Ethics

Many companies set up codes of conduct and develop clear ethical positions on how the firm and its employees will conduct business. The single most effective step a company can take is to demonstrate top management support of ethical standards.

1. **Adopting Written Codes.** Almost all major corporations have written codes of ethics. While business strategies and practices can change, an organization's core principles and values should not.
2. **Instituting Ethics Programs.** Ethical responses can be learned through experience; companies must take the responsibility for educating employees. More and more companies, like Boeing and ExxonMobil, require managers to go through regular ethics training to remind them of the importance of ethical decision making and to update them on current laws and regulations.

Learning Objective 2-2:

Distinguish social responsibility from ethics, identify organizational stakeholders, and characterize social consciousness today.

Social Responsibility

Social responsibility refers to the overall way in which a business itself tries to balance its commitments to relevant groups and individuals in its social environment.

A. The Stakeholder Model of Responsibility

Most companies strive to be ethically responsible to five main groups (organizational stakeholders):

1. **Customers.** Critical factors include charging fair prices, honoring warranties, meeting delivery commitments, and standing behind product quality.

2. **Employees.** Treating workers fairly, making them a part of the team, and respecting their dignity and basic human needs promote a company's reputation.
3. **Investors.** Managers must follow proper accounting procedures, provide appropriate information to shareholders, and manage the organization to protect shareholder rights and investments.
4. **Suppliers.** Partnership arrangements with suppliers can enhance market image and firm reputation. Keeping suppliers informed about future plans, negotiating delivery schedules and prices that are acceptable to both firms build relationships with suppliers.
5. **Local and International Communities.** Contributing to local and global programs has a positive impact on the community.

B. Contemporary Social Consciousness

Views toward social responsibility continue to evolve as managers work to meet the needs of various stakeholders in their business practices.

1. The concept of social responsibility has been developing since the days of **John D. Rockefeller, J.P. Morgan, and Cornelius Vanderbilt**. The concept of accountability was developed.
2. Unfortunately, the recent spate of **corporate scandals** (Enron, bailouts of banks, GM, and Chrysler) colors the public's perception of business in negative hues. However, with growing concerns about climate change and calls for more sustainable business practices, many businesses at least appear to have again moved toward a more responsible approach to doing business. Firms are integrating socially conscious thinking into their production plans and marketing efforts.

Learning Objective 2-3:

Show how the concept of social responsibility applies both to environmental issues and to a firm's relationships with customers, employees, and investors.

Areas of Social Responsibility

A. Responsibility Toward the Environment

Controlling pollution is a significant challenge for contemporary business.

1. **Air Pollution:** Under current laws, many companies must install special devices to limit pollutants they expel into the air. Such efforts are expensive.
2. **Water Pollution:** New legislation and increased awareness of chemical and waste dumping and the resulting dangers has led to improved water quality in many areas of the

country.

3. **Land Pollution:** Proper **toxic waste** disposal and recycling programs are allowing companies to help restore land quality and to prevent further contamination. **Recycling**, the reconversion of waste materials into useful products, has become an issue not only for municipal and state governments but also for many companies engaged in high waste activities.

B. Responsibility Toward Customers

1. **Consumer Rights:** Consumerism is social activism dedicated to protecting the rights of consumers in their dealings with businesses.
2. **Unfair Pricing:** Collusion occurs when two or more firms agree to collaborate on wrongful acts, such as *price fixing*; *price gouging* occurs when firms respond to increased demand with overly steep price increases.
3. **Ethics in Advertising:** Consumers deserve to be given product information that is truthful and not misleading, as well as information that is not morally objectionable.

C. Responsibility Toward Employees

1. **Legal and Social Commitments:** Recruiting, hiring, training, promoting, and compensating are the basis for social responsibility toward employees; a company that provides its employees with equal opportunities without regard to race, sex, or other irrelevant factors is meeting both its legal and its social responsibilities. A **whistle-blower** is an employee who discovers and tries to end a company's unethical, illegal, or irresponsible actions by publicizing them. Most organizations now have whistleblower policies to protect whistleblowers from retaliation.

D. Responsibility Toward Investors

Financial Mismanagement: Insider trading occurs when someone uses confidential information to benefit from the purchase or sale of stocks. Misrepresentation of finances is where unethical managers project profits that they do not expect to get or hide losses and expenses incurred to boost paper profits. **Misrepresentation of finances:** In maintaining and reporting its financial status, every corporation must conform to generally accepted accounting principles.

Learning Objective 2-4:

Identify four general approaches to social responsibility and note the role of social responsibility in small business.

Implementing Social Responsibility Programs

A. Approaches to Social Responsibility

1. **Obstructionist Stance:** Organizations do as little as possible to solve social or environmental problems, have little regard for ethical conduct, and will go to great lengths to deny or cover up wrongdoing.
2. **Defensive Stance:** Organizations will do everything that is required of them legally but nothing more.
3. **Accommodative Stance:** The organization meets its legal and ethical requirements but will also go further in certain cases, such as if it can be convinced that given programs are worthy of its support.
4. **Proactive Stance:** Firms that adopt this approach take to heart the arguments in favor of social responsibility, view themselves as citizens in a society, indicate sincere commitment to improve general social welfare, and surpass the accommodative stance by proactively seeking opportunities to contribute.

B. Social Responsibility and the Small Business

Many big-business responses to ethical and social responsibility issues apply to small businesses; differences are primarily differences of scale. Small business owners are faced by the same ethical dilemmas as the large companies that we more frequently read about. It is important that small companies develop ethical policies and procedures like their larger counterparts. A key to business success is to decide in advance how to respond to the issues that underlie all questions of ethical and social responsibility.

Learning Objective 2-5

Explain the role of government in social responsibility in terms of how governments and businesses influence each other.

The Government and Social Responsibility

An especially important element of social responsibility is the relationship between business and government.

A. How Governments Influence Business

The government (national, state, or local) attempts to shape social responsibility practices through both direct and indirect channels. Direct influence most frequently is manifested through *regulation*, whereas indirect influence can take a number of forms, most notably taxation policies.

1. **Direct Regulation:** The government most often directly influences organizations through **regulation**, the establishment of laws and rules that dictate what organizations can and cannot do. This **regulation** usually evolves from social beliefs about how businesses should conduct themselves. Another approach that governments can use to regulate business practices is through legislation.
2. **Indirect Regulation:** Other forms of regulation are **indirect**. For example, the government can indirectly influence the social responsibility of organizations through its tax codes. In effect, the government can influence how organizations spend their social responsibility dollars by providing greater or lesser tax incentives.

B. How Business Influences Government

Just as governments can influence businesses, so too can businesses influence the government.

1. **Personal Contacts:** Because many corporate executives and political leaders travel in the same social circles, personal contacts and networks offer one method of influence.
2. **Lobbying:** **Lobbying**, or the use of persons or groups to formally represent an organization or group of organizations before political bodies, is also an effective way to influence the government.
3. **Political Action Committees:** **Political action committees (PACs)** are special organizations created to solicit money and then distribute it to political candidates.
4. **Favors:** Organizations sometimes rely on **favors** and other influence tactics to gain support. Although these favors may be legal, they are still subject to criticism.

Learning Objective 2-6

Discuss how businesses manage social responsibility in terms of both formal and informal dimensions and how organizations can evaluate their social responsibility.

Managing Social Responsibility

The demands for social responsibility placed on contemporary organizations by an increasingly sophisticated and educated public are stronger than ever. Organizations should view social responsibility as a major challenge that requires careful planning, decision-making, consideration, and evaluation.

A. Formal Organizational Dimensions

1. **Legal Compliance:** **Legal compliance** is the extent to which the organization conforms to local, state, federal, and international laws. Keep in mind, in some instances, perfectly legal accounting practices have still resulted in deception and other problems.

2. **Ethical Compliance:** **Ethical compliance** is the extent to which the members of the organization follow basic ethical (and legal) standards of behavior.
3. **Philanthropic Giving:** **Philanthropic giving** is the awarding of funds or gifts to charities or other worthy causes.

B. Informal Organizational Dimensions

1. **Organization Leadership and Culture:** **Leadership practices** and **organizational culture** can go a long way toward defining the social responsibility stance an organization and its members will adopt. Ethical leadership often sets the tone for the entire organization.
2. **Whistle-Blowing:** **Whistle-blowing** is the disclosure by an employee of illegal or unethical conduct on the part of others within the organization. How an organization responds to this practice often illustrates its stance on social responsibility.

C. Evaluating Social Responsibility

To make sure their efforts are producing the desired benefits, any business that is serious about **social responsibility** must apply the concept of control to social responsibility. Many organizations now require all employees to read their guidelines or **code of ethics** and then sign a statement agreeing to abide by it. A business should also evaluate how it responds to instances of questionable legal or ethical conduct.

More formally, an organization may actually evaluate the effectiveness of its social responsibility efforts. Additionally, some businesses occasionally conduct a **corporate social audit**, a formal and thorough analysis of the effectiveness of a firm's social performance.