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October 31, 2014

Business Ethics | BUS-L 375

**When Does Corporate Responsibility Stop?**

**Introduction**

In February 2000, Starbucks’ annual shareholder’s meeting had an unpleasant gathering; however, the companies’ financial situation was not the center focus. In fact, Starbucks led the retail coffee industry in sales and customer loyalty letting the company reach 88th on *Business Week’s*  “Best Global Brands.” Starbuck’s concern was the non-governmental organization, Global Exchange, which threatened to start a national Anti-Starbucks campaign if they didn’t start offering fair trade coffee. They criticized Starbucks for profiting at the coffee farmer’s expense by paying low prices and not buying fair trade coffee beans. Fair trade is the practice of giving farmers fair and equal rights and working conditions for a fairly priced work. Starbucks faced the private political fight for public opinion on it’s coffee sourcing, a battle it will want unpublished and has never been mentioned in its investor reports.

By 2000, the growing $80 billion coffee industry started receiving importance in fair trade discussions as coffee was second only to oil as the world’s most traded commodity. The leading coffee producers comprised mostly of small, independent farms with 50 - 70 percent of global coffee production. These independent farmers do not usually own equipment to process the coffee and consequently have little negotiating power. Middlemen provide high interest rate credit to the farmers to get the harvest to market. Commodity prices shift frequently, so these farmers carry overwhelming price risk. At the time, a coffee oversupply left price levels at a 50 year low; 26 cents lower than the 1998 price of $1. The high interest rates and price risks left little hope for any financial stability for the farmers. In 2000, Starbucks paid $1.20 per pound for high quality as opposed to the $0.86 industry average. The coffee industry had many layers between suppliers and end-consumers, leaving the farmers with even less compensation.

Starbucks brought in a profit and the company had a strong social responsibility built into it’s culture. Starbucks even had a history with working with NGOs starting in 1996. The Starbucks brand carried great weight, oftentimes out competing existing coffee shops when entering new locations. Global Exchange most likely targeted Starbucks because of these reasons. Starbucks marketed itself as a socially responsible company. The corporate mission statement and values showed a strong ethical awareness. The company was 46th on the “100 Best Corporate Citizens” from *Business Ethics* and 88th on *Fortune’s* “100 Best Companies to Work for.” The company has a significantly lower turnover rate in the retail coffee industry with a full two months of training for new employees. Starbucks put “people first and profits last” and their mission statement followed that belief. The company created an Environmental Affairs component, hiring a director in 1994. Starbucks annually donates millions to CARE, an organization to help developing nations, and partners with Conservation International for protection of the environment in coffee growing nations.

In 2000, fair trade coffee had five qualifications according to TransFair USA. First, A fair price floor for the coffee with $1.26 per pound of regular and and $1.41 for organic. Second, producers must belong to democratic associations organized by membership. Third, importers must build long-term and stable relationships with the coffee growers and have direct trade. Fourth, producers should receive up to 60% of financing from importers. Fifth, producers must grow their crops by implementing environmental protection.

Starbucks Mission and Values

OUR MISSION

Establish Starbucks as the premier purveyor of the finest coffee in the world while maintaining our uncompromising principles while we grow.

The following six guiding principles will help us measure the appropriateness of our decision:

* Provide a great work environment and treat each other with respect and dignity.
* Embrace diversity as an essential component in the way we do business.
* Apply the highest standards of excellence to the purchasing, roasting, and fresh delivery of out coffee.
* Develop enthusiastically satisfied customers all of the time.
* Contribute positively to our communities and our environment.
* Recognize that profitability is essential to our future success.

OUR VALUES

With our partners, our coffee and our customers at our core, we live these values:

* Creating a culture of warmth and belonging, where everyone is welcome.
* Acting with courage, challenging the status quo and finding new ways to grow our company and each other.
* Being present, connecting with transparency, dignity and respect.
* Delivering our very best in all we do, holding ourselves accountable for results.
* We are performance driven, through the lens of humanity.

Source: Starbucks website

**Identifying Key Players**

Starbuck’s decision could affect many people internally and externally. Orin Smith, the CEO at the time, would have to act out the decision he makes. Smith must steer the company in the direction that he chooses that could impact the company for years. Starbucks employees, and all future employees such as current CEO Howard Schultz, will have to implement and work with the decision going forward. Employees will interact with suppliers and end customers, who are all affected by the implementation of fair trade.

Starbucks employees must realize their role in others lives, such as the small coffee farmers. These farmers have a stake in the decision, since they could gain financial independence and control over their business if Starbucks moved towards fair trade. Starbucks customers have relied on the high quality coffee they pay for; any changes to how Starbucks obtains the coffee beans will affect them.

The non-governmental organizations and activists will want to see their efforts pay off. If Global Exchange can make an impact, it can grow and move to other issues. TransFair USA, the organization who developed the fair trade definition, hopes to see the guidelines followed.

Hosmer’s Moral Reasoning Process

**Identifying the Moral Problem**

Starbucks faces a decision on whether or not to respond to the demands of Global Exchange and begin to purchase and use fair trade coffee in their coffee shops. Most likely, Starbucks carries some loss aversion to losing profits and reputation. This is a moral issue because the decision to star fair trade could damage Starbuck’s profits through poor coffee quality, and Starbucks may feel their moral equilibrium allows for them to continue to profit. Quality coffee has allowed Starbucks to build a coveted reputation, and risking that quality will stress the organization. If Starbucks decides against using fair trade coffee, small-scale farmers will still fight against getting taken advantage of and facing an endless cycle of poverty. If Starbucks chooses to pursue fair trade coffee, it could be viewed as giving in too easily into activist’s demands and could get taken advantage of by other non-governmental organizations in the future. Starbucks built relationships with suppliers through years of business, implementing higher standards could damage reputation and these relationships.

Starbucks faces the dilemma of “when have we done enough?”, essentially overconfidence bias towards their outstanding historic corporate responsibility. As the leader in the coffee industry’s price and social responsibility, why should Starbucks do more? Global Exchange wants Starbucks to lead the industry further and make its standards higher. Starbucks does have the power to positively impact the lives of the farmers, and this may outweigh any minor profit loss. The company promotes itself as putting “people first and profits last”, but the general public will not feel or require this change. Starbucks could continue on, but know that it may have not put *all* people first. Starbucks must deal with the conflict of interest between shareholders and stakeholder and recognize its framing as a skew to that viewpoint.

**Additional Facts**

The following questions touch on some of the additional facts unknown to Orin Smith at the time of the decision that could assist in making a decision on how to solve the dilemma.

* What is the quality of these fair trade coffee beans?
* Has Global Exchange done a fundamental attribution error to the real problem?
* How much of a positive impact will fair trade really have on the suppliers?
* Would we have known about the small-scale farmers if Global Exchange had not pressed the issue? Would starbucks have suffered from moral myopia otherwise?
* How will this decision impact the supply chain?
* Will our customers and/or investors support fair trade coffee?
* How else could our resources and efforts be used in another area of business?
* Can the small-scale farms produce enough coffee beans to meet demand?
* Will Starbucks customers pay the same price?

**Available Alternatives**

With freedom to use moral imagination, Starbucks had numerous alternatives available at the time of their first decision. As stated earlier, the first decision that Starbucks made to mitigate some threats by the Global Exchange was to sell fair trade coffee in their domestic stores and re-evaluate the decision in a year. Some alternatives included: ignoring the NGO and continuing to sell premium coffee, fighting back against the NGO, or giving in completely to Global Exchange. Each of these options has its drawbacks. Doing nothing would ultimately infuriate Global Exchange and force them to continue to pressure the company further. Fighting back would go against the socially responsible values of the company and would likely create more negative press. Giving in to the NGO worried Starbucks because if they gave in to this campaign, they feared they would be viewed as an “easy target” for other activist groups in the future. Starbucks could meet Global Exchange halfway and bring up their standards, but not all the way to the high standards of fair trade. Starbucks could test fair trade to some degree, as a means to check the impact fair trade would have on the business and farmers.

**Identifying Personal Impacts**

Starbucks CEO Orin Smith had to analyze and weigh-out several personal impacts before making any decision surrounding this issue. There were some obvious impacts to the business no matter what route he chose. If Smith decides to ignore the NGO, he knew that because they were so adamant on this issue and had success in the past with other companies like Nike, Global Exchange would not just drop the issue. Global Exchange would likely continue its Anti-Starbucks campaign, bringing more negative press and ultimately causing more problems in the future that he would not be able to ignore. Global Exchange does run the risk of the fundamental attribution error, and placing too much weight on Starbucks for the small farmers’ problems. If Smith decides to begin using fair trade coffee, he will create more hard costs for the company by having to pay a higher price for regular and organic fair trade coffee. Higher costs will reduce profit margins, which will put his job at jeopardy if shareholders disagree with the results of the switch.

Smith’s personal family would also be impacted by his decision. Deciding not to pursue purchasing fair trade coffee could prove to not only affect his business, but his family life as well. The media and activist will most likely question any decision he makes, or fails to make. Activists can write letters to the family members and the media can broadcast and publish personal details that could be aggravating and invasive for the family. This can strain his family relationships and bring work home for him.

Some psychological impacts from this could be that he feels he made a difference with his life. He could feel a newfound sense of self-worth, as he made a positive impact in the world. Leaving the status quo the same may haunt him, as he could feel guilt. He does not want to fall into a failing role morality, believing his role as CEO allows for him to act in this way.

Some tests that Smith could apply to this situation are the Metaphor of the Ledger and the Newspaper test. The Metaphor of the Ledger weighs out how many good things you have done against how many bad things and then you can decide if you can “afford” to make a less ethical decision and still feel that the good outweighs the bad. In this situation, Smith could personally use this tactic to see if after making a decision regarding this issue, he still feels he has done enough good or needs to improve. He could also use a tactic that involves having the decision be the headline of the Daily Herald the next day. Would he want his final decision to be the first thing that everyone reads about the following day? These psychological tests are a good way for Smith to double check if he is making the most moral decision.

**Applying Moral Frameworks**

The most important step in Hosmer’s model is the fifth step of applying the 3 modern business moral frameworks to the moral issue that is in question. The three frameworks are Shareholder Theory, Stakeholder Theory, and Virtue Theory.

*Shareholder*

Shareholder Theory is essentially making the benefit of shareholders of the company the most important factor when making a moral decision. In more concrete terms, Friedman states that “In a free-enterprise, private-property system, a corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in ethical custom”. Drilling this down, he is basically saying that it is the responsibility of a CEO and other executives to make decisions that benefit their employers, or the shareholders, while abiding by associated laws in an ethical manner. Some would criticize this framework by saying that if a company or decision-maker puts shareholders first, they made the decision out of greed. This framework focuses on the bottom line and if a greedy CEO makes a decision “for his shareholders”, but in reality, just for himself, this could prove to be the wrong choice down the road for the company or stakeholders if he didn’t weigh-out the costs and benefits fully through the whole Hosmer process. We can see an example of this in the Enron case discussed in class.

When applying the first moral framework, Shareholder theory, to Starbucks and the Global Exchange case, the most important factor to consider is the shareholder’s benefit in the form of profits. The NGO was pressuring Starbucks to buy from small farmers directly and to give them a fair price on their coffee beans. In 2000, Starbucks was paying a premium price of $1.20 per pound of coffee beans while the market price was just above 64 cents per pound. This market price was extremely low because at this time there was a high oversupply of coffee beans with no sign of any improvement in the near future. The small farmers received an even smaller portion of the already rock-bottom price because there were several layers between the farmer and consumer, including unfair middlemen known as “coyotes” who would give a cash advance to farmers before harvest attached with credit that had high interest rates in exchange for bringing their beans to market, which provided the farmers with a low profit right off the bat.

Based on the definition of fair trade coffee given by the TransFair USA, includes a price of $1.21 per pound of regular coffee and $1.41 for certified organic coffee. This new price for fair trade coffee was one cent higher than the premium price that Starbucks was already paying for coffee. Although this may not seem like a large number, based on the number of pounds of coffee that Starbucks buys per year, given on the Starbucks website, this creates an extra $3 million of purchasing costs which will obviously decrease the bottom line. That is just for their regular coffee purchases, 4.4 million pounds of organic coffee would create almost another million dollars spent in just purchasing the coffee beans. This almost $4 million in extra costs will negatively impact the benefits of the shareholders.

As a publicly traded company, Starbucks has many diversified debt and equity holders. Reasonably, most of these shareholders would like to see strong financial health for Starbucks. But in this situation, profits may only decline slightly for the switch to fair trade. These investors understand the corporate culture of starbucks as a socially responsible company, and they invested in this belief. Many of the investors themselves may have social responsibility beliefs, and Starbucks should act in their best interests. The question now remains, is the profit loss value less than the value of the social impact? Since Starbucks has proven profitable, implementing more social responsibility might be worth it, since the investors expect it as they invested in the corporate responsibility of Starbucks as well.

*Stakeholder Theory*

The second modern framework is Stakeholder Theory. At a basic level, this theory explains that the interests of the stakeholders of the company should be the main factor when making a decision even if the decision reduces company profitability. Investopedia defines a stakeholder as “A party that has an interest in an enterprise or project. The primary stakeholders in a typical corporation are its investors, employees, customers and suppliers. However, modern theory goes beyond this conventional notion to embrace additional stakeholders such as the community, government and trade associations” This theory encompasses shareholders as explained by Investopedia’s definition, but does not make them the only group to consider. There is also a formula given to us in our class book, *The Vision of the Firm,* by Timothy Fort. This formula gives a guide on how to prioritize among the many stakeholders in a company given as:

**EBB = Rk + Jr + U** where ethical business behavior equals the basic and non-basic Rights of the stakeholders plus Justice, made up of equality and social contract, plus Utilitarianism, which says that actions are right if they are useful or for the benefit of a majority. We will use this formula when evaluating Starbucks’ stakeholders. Placing too much emphasis on the stakeholders may benefit the customers or the suppliers but could negatively affect the company’s profitability or anger the shareholders. We see an example of extreme stakeholder theory with the new company, Alibaba. That company puts customers first, employees second, and shareholders last out of the three. Despite this, the company still boasts high profits, but this is not always the case and will we see if this new company can continue to show high profits while keeping this mentality.

Applying the second framework of Stakeholder Theory, the decision-maker caters to the benefits of all stakeholders. Starbucks’ stakeholders includes their employees, customers, Global Exchange, the small farmers, original suppliers, and investors. All of these groups are obviously highly important to the company based on the mission statement and the specifics of this case. Prioritizing the most important stakeholder(s) is a daunting task considering there are conflicts between some of them. At this point, if we put ourselves in the decision-maker(s) shoes, we would use the formula to decide who would be the highest regarded among the rest and then rank the remaining.

Right away, we can assume that investors are not going to be the highest regarded because this method is contained in Shareholder Theory. Employees, customers and original suppliers, although immensely important, are not number 1 because in this case, Global Exchange and the situation of the small farmers are putting pressure on Starbucks to make this moral decision. We decided that the small farmers are the highest regarded in terms of stakeholders because they are the reason why this case exists. They obviously have basic and non-basic rights to make a living and provide for their families without the risk of losing massive amounts of profits to the many layers between them and the consumer. There is a need for justice as well considering that 50% - 70% of global coffee comes from small-scale farms (California Management Review pg. 97) and the farmers are the ones most negatively affected by the normal purchasing logistics. In line with that, a utilitarianistic view would imply that hundreds of thousands of small farmers would benefit greatly from a Fair Trade Agreement.

The rest of the stakeholders were ranked in this order based on our calculations: Global Exchange, customers, original suppliers, investors and employees. Global Exchange is ranked second because they were the ones that brought this issue to the attention of Starbucks and are highly in favor of helping the primary stakeholder of the small farmers. The rest are ranked based on the original components of the formula and how greatly they will be affected by a decision to buy fair trade coffee.

*Virtue Theory*

The third and final framework is Virtue Theory. When this theory is applied, the decision-maker attempts to make the most ethical decision in the situation based on several pre-determined virtues identified by the decision-maker. Virtue Theory essentially has three steps when applying. The first is to identify relevant virtues applicable to the moral issue, the next is to define those virtues, and finally, apply those virtues to the moral issue. We see an example of this in our class discussion of the hypothetical case on Steve Lewis. Lewis is a black analyst at a company and is asked to attend a client meeting to persuade another company to do business with them, but it is only because they would like to show diversity even though he isn’t allowed to be part of this meeting. A virtue going against this would be honesty. The company should not try to manipulate the other by falsely showing diversity. Those who criticize this theory would say that people caught up in always making the most “ethical” decision will eventually make an ethical decision that isn’t in the best interest of the company or stakeholders.

Virtue Theory is the final framework given in Hosmer’s model to be applied. Again, putting ourselves in the position of Starbucks, we must first identify relevant virtues applicable to the moral issue. Some virtues that continued to prevail as we discussed were social responsibility, compassion, profitability, justice, excellence, and satisfied customers.

Next we must define these virtues and apply them to the moral issue in the context of the case. Social responsibility is one of the main points in the mission statement of Starbucks and is the corner-stone of this case. Being socially responsible in this case means that Starbucks should cater at least partially to the demands of Global Exchange to help the farmers in their state of near poverty by purchasing some of their coffee from these small farmers directly to ensure that they receive proper compensation. Compassion and justice directly tie in with this previous virtue. Being compassionate means to show sympathy and concern for others. Related to this case, Starbucks should be compassionate to these farmers by recognizing that they are living in an unjust cycle of business and giving them proper compensation for their harvest. Justice also goes hand-in-hand with this in that Starbucks can bring justice to these farmers by signing an agreement to purchase from them making the suppliers more equal in terms of profits.

Profitability is a virtue held in high regards in the mission statement of Starbucks and they recognize that they must be profitable to ensure future success. In terms of this case, to maximize profitability, Starbucks should not agree to the demands of Global Exchange and either ignore them or fight back.

Excellence is also a virtue encompassed in Starbucks’ mission statement. They define excellence in terms of having high standards of purchasing, roasting, and delivery of their coffee. Related to this issue, we believe that Starbucks is hesitant to agree to buy fair trade coffee because they are not sure that these are the best coffee beans available and this conflicts with a major point of their mission statement. They want to be sure that these coffee beans are up to “excellent” standards and this is why they decided to do a trial by purchasing and brewing fair trade coffee once a month in domestic shops for a year.

Satisfied customers is something that Starbucks strives for continually while conducting business. They strive for excellent customer service by giving customers total freedom to customize their drinks and replace a drink that they made incorrectly. This case also touches on this virtue and is related to excellence. Starbucks fears that this coffee is not up to their high standards and would negatively affect the customer’s satisfaction. They are also worried that these small farmers would not be able to keep up with Starbucks’ high demand for coffee beans and would not have enough coffee to satisfy customer demand.

*Total Integrity Management*

Total Integrity Management is a strategy to proactively create a culture of trust within the organization and with the public that prevents future ethical dilemmas, as defined in class. TIM is grouped into 3 separate categories, Hard trust, Real trust, and Good trust. Hard trust is complying with the law so long as it’s just. Real trust is the same as the stakeholder formula where we align rhetoric and incentives: it is comprised of rights, justice and utilitarianism. Good trust is made up of corporate motivation or the desire by people to act ethically by nature and to do good for the community or corporation.

Related to Starbucks, the company seems to have an ethical corporate culture already. This goes back to the mission statement again: they want to be profitable while maintaining high customer satisfaction and being socially responsible. In the end, Starbucks made the ethical decision by first trying to use fair trade coffee and eventually uniting with other organizations to further expand their use of ethically sourced coffee and plans to have 100% ethically certified coffee by 2015. They made this decision basically on their own without much NGO interference, implying a relatively ethical corporate culture.

**Conclusion**

We recommend that Starbucks should take the action of agreeing to buy fair trade coffee from these small-scale farmers because this socially responsible action is in line with their mission statement and brings more benefit to a higher majority of stakeholders in desperate need of solid profits. The profit loss of approximately $4 million by making this decision is miniscule compared to the overall revenues that Starbucks receives every year, which were about $2 billion at the time of the decision.

Starbucks eventually made the decision after the year-long trial period ended to continue brewing fair trade coffee and also expand its social responsibility programs and research other alternatives to fair trade all to improve the livelihood of the small scale farmers. Initiatives include purchasing “green coffee” at outright prices, creating direct relationships and creating long-term contracts with suppliers. Despite numerous actions and socially responsible awards, Global Exchange still didn’t believe that Starbucks was being responsible enough.

Starbucks then paired with Oxfam America, the Oaxacan State Coffee Producers Network and the Ford Foundation with these goals:

· Increase supply of High-quality fair trade coffee for US from small farmer co-ops

· Improve skills of small farmers by training and giving resources

· Provide information and support to enable farmers to earn premium prices

· Enable farmers to disseminate their learning to other coffee co-ops

They made some great progress and continue to do so. Starbucks states clearly on their website that they want to have 100% ethically sourced coffee by 2015 and they had some fantastic progress in 2012:

2012 progress was that 93% of coffee is ethically sourced

· 1.6% organic certified

· 8.1% was fair trade certified

· 90% Coffee and Farmer Equity certified

In the end, we believe that Starbucks went about this decision in an ethical manner, keeping all stakeholders and other’s affected in mind. Having the trial period to see if Starbucks could maintain high standards of coffee while brewing fair trade was a great way to slowly become acclimated to using it later. After this period they continued to find new ways to help the small-scale farmers other than fair trade and with a little more push from Global Exchange, were able to have a majority of their coffee originate from ethical sources. Starbucks made the best decision for the most amount of people and continue to be successful in business today with high hopes to continue their ethical practices long into the future. Fighting through ethical fading, loss aversion, and a seemingly positive moral equilibrium, Starbucks used it’s moral imagination to help lead the entire coffee industry to better business practices and aid the exploited coffee farmers.