Chapter 9

Strategy: Core Concepts and Analytical Approaches

Chapter 9
Strategy, Ethics, and Social Responsibility

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Chapter Learning Objectives

1. Understand where ethical standards come from and to critically consider whether and why businesses and their personnel should be ethically accountable for their behavior.
2. Become aware of the principal reasons why companies sometimes pursue unethical strategies and why businesspeople sometimes engage in unethical conduct.
3. Learn why unethical business conduct can be very costly for a company’s shareholders.
4. Gain a strong understanding of the concepts of corporate social responsibility, corporate citizenship, and environmental sustainability.
5. Become familiar with both the moral case and the business case for socially responsible business behavior.

Key Topics Covered in Chapter 9

- What Do We Mean by Business Ethics?
- Where Do Ethical Standards Come From – Are They Universal or Dependent on Local Norms?
- The Three Categories of Management Morality
- Drivers of Unethical Strategies and Business Behavior
- Why Should Company Strategies Be Ethical?
- Strategy, Social Responsibility and Corporate Citizenship
Business ethics is the application of ethical principles and standards to the actions and decisions of business organizations and the conduct of their personnel.

Ethical principles in business are not different from ethical principles in general.

The actions of businesses and businesspeople are judged by society’s standards of what is morally right and wrong.

- Not by a special set of rules that apply to business conduct
- If dishonesty is considered unethical and immoral, then dishonest behavior in business is unethical
- If society deems bribery unethical, then it is unethical for company personnel to offer payoffs or kickbacks to obtain sales or other favors

Are Ethical Standards Universal or Dependent on Local Norms?

Three schools of thought regarding how ethical standards are determined:

- Ethical Universalism
- Ethical Relativism
- Integrative Social Contracts Theory

The School of Ethical Universalism

According to the school of ethical universalism . . .

- the most important concepts of what is right and what is wrong are universal and transcend most all cultures, societies, and religions
- For instance, being truthful (or not lying or not being deliberately deceitful) strikes a chord of what’s right in the peoples of all nations
- The same is true for demonstrating integrity of character, not cheating, and treating people with courtesy and respect
- In most societies, people would concur that 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.

Such common moral agreement about right and wrong actions and behaviors across multiple cultures and countries gives rise to universal ethical standards that apply to members of all societies, all companies, and all businesspeople.
Examples of Universal Ethical Principles or Norms

- Honesty
- Trustworthiness
- Respecting rights of others
- Practicing the Golden Rule
  - Treating people with dignity and respect
- Exercising due diligence in product safety
- Acting in a manner that does not
  - Harm others or put them at risk (as concerns safety) or endanger the environment

What Is the Strength of the Ethical Universalism Approach to Establishing Ethical Standards?

- Ethical universalism draws upon the collective views of multiple societies and cultures to put some clear boundaries on what constitutes ethical and unethical business behavior and irrespective of the country or culture in which a company’s personnel are conducting activities.
- When basic moral standards do not vary significantly from country to country, a multinational company can
  - Apply a code of ethics more or less evenly across its worldwide operations
  - 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...

- 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 locally prevailing ethical standards.
- There is no “one-size-fits-all” template for judging the ethical appropriateness of business actions and the behaviors of company personnel
**Ethical Relativism and the Use of Underage Labor**

- 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 guide to ethical behavior. This can be ethically dangerous.
- In industrialized nations, the use of "underage" workers is considered taboo.
- But in 100-plus countries, it is customary to view children as potential, even necessary, workers.
- According to ethical relativism, whether the use of underage labor is ethically right or wrong depends on what country one is in.

  - If the use of underage labor is to be ethically forbidden and children in many poverty-stricken countries are not permitted to work, they may be forced to seek work in lower-wage jobs in "hidden" parts of the economy, or be put on the streets begging or even reduced to trafficking in drugs or engaging in prostitution.

- Is this better than allowing the use of underage labor?

**Ethical Relativism and the Payment of Bribes and Kickbacks**

- In some countries, the payment of bribes and kickbacks is normal and customary; in other countries such payments are illegal, as well as unethical.
  - The Foreign Corrupt Practices Act prohibits U.S. companies from paying bribes in all countries where they do business, even if such payments are customary.
- Companies forbidding payment of bribes in their codes of ethics face a formidable challenge in countries where such payments are entrenched as a local custom.
  - Refusing to pay bribes or kickbacks in these countries (so as to comply with the company's code of ethical conduct) often means losing sales to competitors willing to make such payments.
  - But going along with the payment of bribes or kickbacks undercuts enforcement of and adherence to the company's code of ethics.

- So should a company observe ethical principles or wade into the moral quicksand of paying bribes to win sales?

**Applying the Principle of Ethical Relativism in Business Situations Is Problematic**

- Relying upon the principle of ethical relativism to judge the ethical appropriateness of business conduct is morally troublesome.
  - If a country's culture is accepting of bribery or environmental degradation or exposing workers to dangerous conditions or the use of child labor, should the ethical bar for businesses be lowered to permit or condone such actions and conduct?
- Relying upon ethical relativism poses a real dilemma for multinational companies.
  - A multinational company that takes the position of permitting company personnel to pay bribes and kickbacks or use underage labor in countries where such actions are customary but forbids company personnel from engaging in such actions where they are unethical or illegal has little moral basis for enforcing ethical standards companywide.

- Rather, the clear message to employees is that the company has no ethical standards or principles of its own, preferring to let its practices be governed by the countries in which it operates.

- Having multiple sets of ethical standards without some kind of higher order moral compass is a slippery slope to negotiate.
According to integrative social contracts theory, the ethical standards a company should try to uphold are governed by:

- A limited number of universal ethical principles that are widely recognized as putting legitimate ethical boundaries on actions and behavior in all situations and
- The circumstances of local cultures, traditions, and shared values that further prescribe what constitutes ethically permissible behavior and what does not.

But universal ethical norms take precedence over local ethical norms.

Universal ethical agreements about what is morally right and wrong form a contract with society (a “social contract”) 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.

In instances involving universally applicable ethical norms (like paying bribes), there can be no compromise on what is ethically permissible and what is not.

But these universal ethical principles still leave some “moral free space” for the people in a particular country (or local culture or group) to specify what other actions may or may not be permissible within the bounds defined by universal ethical principles.

However, local or second-order ethical norms never take precedence over universal ethical principles or norms.

Integrated social contracts theory 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.
  - In many instances of cross-country differences, one side is likely to be more “ethically correct” or “more right” than another.
Chapter 9: PowerPoint Slides

The Three Categories of Management Morality

- Managers that are **moral**
- Managers that are **immoral**
- Managers that are **amoral**

Traits of a Moral Manager

- Dedicated to high standards of ethical behavior in
  - Own actions
  - How the company’s business is to be conducted
- A steward of ethical behavior
- 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
- Regard complying with the law as an ethical minimum and have a habit of operating well above what the law requires

Traits of an Immoral Manager

- Has no regard for ethical standards in business
- Pays no attention to ethical principles in making decisions and conducting the company’s business
- Believes good businesspeople cannot spend time watching out for the interests of others and agonizing over “the ethically correct thing to do”
- Thinks nice guys come in second and the competitive nature of business requires that you either trample on others or get trampled yourself
  - What really matters is single-minded pursuit of one’s own best interests
- Has few scruples, little or no integrity, and is willing to do most anything if unlikely to be caught
  - May even be willing to short-circuit legal and regulatory requirements
Are of the strong opinion that 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 rules and regulations, then they should not be seen as unethical. 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. However, observing some higher ethical considerations may be appropriate in life outside of business. A concept of right and wrong that is lawyer-driven: “How much can we get by with?” “What are the risks of going ahead if a particular action is borderline?”

Evidence indicates a sizable majority of managers are either Amoral or Immoral. Recent issues of the Global Corruption Report indicate corruption is widespread across the world.

Large numbers of immoral and amoral business people

Overzealous pursuit of personal gain, wealth, and other selfish interests

Heavy pressures on company managers to meet or beat earnings targets

Company cultures that place profits and good performance ahead of ethical behavior
People obsessed with wealth accumulation, greed, power, status, and other selfish interests often
► Push ethical principles aside in their quest for self gain
► Exhibit few qualms in
  • Skirting the rules or
  • Doing whatever is necessary to achieve their goals
► Engage in all kinds of unethical strategic maneuvers and behaviors

Managers often feel enormous pressure to do whatever it takes to deliver good financial performance
► Often their compensation depends heavily on company performance
► As the pressure builds, they start stretching the rules further and further, until the limits of ethical conduct are overlooked.
► Once ethical boundaries are crossed in efforts to “meet or beat their numbers,” the threshold for making more extreme ethical compromises becomes lower

In an ethically corrupt or amoral work climate, people have a company-approved license to
► Ignore “what’s right”
► Engage in most any behavior or employ most any strategy they think they can get away with
► Pressures to conform to cultural norms can prompt otherwise honorable people to
  ► Make ethical mistakes
  ► Succumb to the many opportunities to engage in unethical practices
Why Should Company Strategies Be Ethical?

Two reasons:

- Because a strategy that is unethical in whole or in part is morally wrong and reflects badly on the character of the company personnel involved.
- Because an ethical strategy is good business and in the self-interest of shareholders.

The Moral Case for an Ethical Strategy

Moral managers believe unethical strategies are morally wrong.

- Ethical strategy-making generally begins with managers that have strong moral character and truly care about conducting the company's business in an honorable manner.
- Managers with high ethical principles and standards are usually advocates of a corporate code of ethics and strong ethics compliance.
  - They are genuinely committed to certain corporate values and business principles.
  - They walk the talk in displaying the company's stated values and living up to its ethical standards.
  - They believe ethical standards should paint the white lines for a company's actual strategy and business conduct.
- As a consequence, ethically strong managers consciously opt for strategic actions that can pass moral scrutiny—they display no tolerance for strategies with ethically controversial components.

The Business Case for Ethical Strategies

- Deliberate pursuit of unethical strategies and tolerance of unethical conduct is a risky practice from both a shareholder perspective and a reputational standpoint.
- A company can incur large and burdensome costs when unethical behavior on its part is discovered, the wrongdoings of company personnel are headlined in the media, and it is forced to make amends for its behavior.
- The more egregious are a company's ethical violations,
  - The higher the costs
  - The bigger the damage to its reputation (and to the reputations of the company personnel involved).
  Shareholders suffer major damage.
The Concepts of Social Responsibility and Good Corporate Citizenship

- The essence of socially responsible business behavior is that a company should balance strategic actions to benefit shareholders against the duty to be a good corporate citizen.
- The underlying thesis is that a company and its managers have a duty to:
  - Display a social conscience in operating the business.
  - Take into account how managerial decisions and company actions affect the well-being of employees, local communities, the environment, and society at large.

What Does Acting in a Socially Responsible Manner Entail?

Socially responsible behavior and good corporate citizenship entails:
- Efforts to employ an ethical strategy and observe ethical principles in operating the business.
- Making charitable contributions, donating money and the time of company personnel to community service endeavors, supporting various worthy organizational causes, and reaching out to make a difference in the lives of the disadvantaged.
- Actions to protect or enhance the environment and, in particular, to minimize or eliminate any adverse impact on the environment stemming from the company’s own business activities.
- Actions to create a work environment that enhances the quality of life for employees and makes the company a great place to work.
- Actions to build a workforce that is diverse with respect to gender, race, national origin, and perhaps other aspects that different people bring to the workplace.

Figure 9.1: The Costs Companies Incur When Ethical Wrongdoing Is Found Out

<table>
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<tr>
<th>Visible costs</th>
<th>Internal administrative costs</th>
<th>Intangible or less visible costs</th>
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<td>- Government fines and penalties</td>
<td>- Legal and investigative costs incurred by the company</td>
<td>- Customer defections</td>
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<td>- Civil penalties arising from class-action lawsuits and other litigation aimed at punishing the company for its offense and the harm done to others</td>
<td>- The costs of providing remedial education and ethics training to company personnel</td>
<td>- Loss of reputation</td>
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<tr>
<td>- The costs to shareholders in the form of a lower stock price (and possibly lower dividends)</td>
<td>- The costs of taking corrective actions</td>
<td>- Lost employee morale and higher degrees of employee cynicism</td>
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<td>- Administrative costs associated with ensuring future compliance</td>
<td>- Higher employee turnover</td>
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<td>- Higher recruiting costs and difficulty in attracting talented employees</td>
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<td></td>
<td></td>
<td>- Adverse effects on employee productivity</td>
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<td></td>
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<td>- The costs of complying with often burdensome government regulations</td>
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A company's social responsibility strategy is defined by the specific combination of socially beneficial and community citizenship activities it opts to support with its contributions of time, money, and other resources.

Figure 9.2: The Five Components of a Social Responsibility Strategy

- Protect the environment
- Provide for the longevity of natural resources
- Maintain ecological support systems for future generations
- Guard against ultimate endangerment of the planet

Achievement of such strategies enable a company's operations to be sustainable for centuries.
Example: Unilever’s Environmental Sustainability Strategy

- Tracked 11 sustainability agricultural indicators in its processed foods business
- Launched various programs to improve environmental performance of suppliers
- Reengineered internal processes to improve overall performance on sustainability measures
- Redesigned packaging for many products to conserve natural resources and reduce volume of consumer waste
- Addressed societal needs of consumers in developing countries

Moral Case: Corporate Social Responsibility and Environmentally Sustainable Business Practices

- “It’s the right thing to do.”
  - Ordinary decency, civic-mindedness, and contributing to the well-being of society should be expected of any business
  - Business operates on the basis of an implied social contract with the members of society:
    - Society grants a business the right to conduct its business affairs and agrees not to unreasonably restrain its pursuit of a fair profit for the goods or services it sells.
    - In return for this “license to operate,” a business is obligated to:
      - Act as a responsible citizen
      - Do its fair share to promote the general welfare
- Every company has a moral obligation to be a good corporate citizen.

Business Case: Socially Responsible Behavior and Environmentally Sustainable Business Practices

- Generates internal benefits
  - Enhances recruitment of quality employees
  - Increases retention of employees
  - Improves employee productivity
  - Lowers costs of recruitment and training
- Reduces risk of reputation-damaging incidents, leading to increased buyer patronage
- Works in best interest of shareholders
  - Minimizes costly legal and regulatory actions
  - Provides for increased investments by socially conscious mutual funds and pension benefit managers
  - Focusing on environment issues may enhance earnings
Business Case: Socially Responsible Behavior and Environmentally Sustainable Business Practices

The business reasons why companies should be public-spirited and devote time and resources to social responsibility initiatives, environmental sustainability, and being good corporate citizens:

- Can lead to increased buyer patronage
- Reduces the risk of reputation-damaging incidents
- Yields internal benefits (particularly as concerns employee recruiting, workforce retention, and training costs) and can improve operational efficiency
- Work to the advantage of shareholders