Chapter 3

A. What Is Business Ethics?
   1. The Law as the Standard for Business Ethics
   2. The Notion of Universal Standards for Business Ethics
   3. The Standard of Situational Business Ethics or Moral Relativism
   4. The Business Stakeholder Standard of Behavior

B. Why Is Business Ethics Important?
   5. The Importance of Trust
   7. The Importance of a Good Reputation
   8. Business Ethics and Business Regulation: Public Policy, Law, and Ethics

C. How to Recognize and Resolve Ethical Dilemmas
   9. Categories of Ethical Behavior
   10. Resolving Ethical Dilemmas

Objectives

After studying this chapter, you should be able to

1. Describe the role of ethics in business and law
2. List the methods for recognizing ethical dilemmas
3. Explain the questions to address in resolving ethical dilemmas
4. Understand the importance of ethics in e-commerce
Each day businesspeople work together on contracts and projects. Their completion of the work is partially the result of the laws that protect contract rights. Much of what business people do, however, is simply a matter of their word. Executives arrive at a 9:00 A.M. meeting because they promised they would be there. An employee meets a deadline for an ad display board because she said she would. Business transactions are completed through a combination of the values of the parties and the laws that reflect those values and the importance of one’s word in business. Over time, the rules that govern business, from written laws to unwritten expressions of value, have evolved to provide a framework of operation that ensures good faith in our dealings with each other.

This chapter takes you behind the rules of law to examine the objectives in establishing rules for business conduct. Both social forces and business needs contribute to the standards that govern businesses and their operations.

**A. What Is Business Ethics?**

Some people have said that the term business ethics is an oxymoron, that the word business and the word ethics contradict each other. Ethics is a branch of philosophy dealing with values that relate to the nature of human conduct and values associated with that conduct. Conduct and values within the context of business operations become more complex because individuals are working together to maximize profit. Balancing the goal of profits with the values of individuals and society is the focus of business ethics. Some economists make the point that insider trading on the stock market is an efficient way to run that market. To an economist, insider information allows those with the best information to make the most money. This quantitative view ignores the issues of fairness: What about those who trade stock who do not have access to that information? Is the philosophy fair to them? What will happen to the stock market if investors perceive there is not a level playing field? In the U.S. Supreme Court decision United States v O'Hagan on insider trading, Justice Ruth Ginsburg noted, “Investors likely wouldn't invest in a market where trading based on misappropriated nonpublic information is unchecked.” The field of business ethics seeks to balance the values of society with the need for businesses to remain profitable.

**1. The Law as the Standard for Business Ethics**

Moral standards come from different sources, and philosophers debate the origin of moral standards and which ones are appropriate for application. One set of moral standards is simply what codified or positive law requires. The application of the test of whether an act is legal as a moral standard is common in business. Codified law, or law created by governmental authority, is used as the standard for ethical behavior. Absent illegality, all behavior is ethical under this simple standard. For example, the phrase “AS IS,” when communicated conspicuously on a contract or electronic message (see Chapter 25 for further discussion), means by law that there are no warranties for the goods being sold. For example, if a buyer purchases a used car and the phrase “AS IS” is in the contract, the seller has no legal obligation, in most states, if the transmission falls apart the day after the buyer’s purchase. Following a positive law standard, the
seller who refuses to repair the transmission has acted ethically. However, the issue of fairness still arises. We know there was no legal obligation to fix the transmission, but was it fair that the car fell apart the day after it was purchased?

2. The Notion of Universal Standards for Business Ethics

Another view of ethics holds that standards exist universally and cannot be changed or modified by law. In many cases, individuals feel the universal standards stem from religious beliefs. In some countries today, the standards for business are still determined by religious tenets. Proponents of natural law maintain that higher standards of behavior than those required by positive law must be followed even if those higher standards run contrary to codified law. In the early nineteenth century when slavery was legally permissible in the United States, a positive law standard would sanction such ownership as legal. However, such deprivation of a person’s rights violated the natural law principle of individual freedom and would be unethical. Accordingly, civil disobedience occurs when natural law proponents violate positive law.

Supreme Court Justice Sandra Day O’Connor, who was second in her class at Stanford Law School (Chief Justice William Rehnquist was first), was offered a job as a receptionist for a law firm while her male classmates were hired as attorneys. At that time, no law prohibited discrimination against women, so law firms’ hiring practices, using only a positive law standard, were ethical. However, if the natural law standard of equality is applied, the refusal to hire Sandra O’Connor as a lawyer, a position for which she was qualified, was discriminatory conduct and unethical.

3. The Standard of Situational Business Ethics or Moral Relativism

Situational ethics or moral relativism is a flexible standard of ethics that permits an examination of circumstances and motivation before attaching the label of right or wrong to conduct. The classic example of moral relativism: Would it be unethical to steal a loaf of bread to feed a starving child? A question a Florida court faced was whether to go forward with the prosecution for arson of a man who set fire to an abandoned property in his neighborhood that was used as a crack-cocaine house. In both cases, the law has been broken. The first crime is theft, and the second crime is arson. Neither person denied committing the crime. The issue in both cases is not whether the crime was committed but whether the motivation and circumstances excuse the actions and eliminate the punishment. An employee embezzles money from his employer because he is a single parent trying to make ends meet. Was his conduct unethical? The conduct is illegal, but moral relativism would consider the employee’s personal circumstances in determining whether it is ethical.

Businesses use moral relativism standards frequently in their international operations. Bribery is illegal in the United States, but, as many businesses argue, it is an accepted method of doing business in other countries. The standard of moral relativism is used to allow behavior in international business transactions that would be a violation of the law in the United States.

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natural law—a system of principles to guide human conduct independent of, and sometimes contrary to, enacted law and discovered by man’s rational intelligence.

civil disobedience—the term used when natural law proponents violate positive law.

situational ethics—a flexible standard of ethics that permits an examination of circumstances and motivation before attaching the label of right or wrong to conduct.

moral relativism—takes into account motivation and circumstance to determine whether an act was ethical.
stakeholders–owners of a business who have contributed capital.

downsizing–a reduction in workforce.

stakeholder analysis—the term used when a decision maker views a problem from different perspectives and measures the impact of a decision on various groups.

ETHICS & THE LAW

4. The Business Stakeholder Standard of Behavior

Businesses have different constituencies, referred to as stakeholders, often with conflicting goals for the business. Shareholders, for example, may share economists’ view that earnings, and hence dividends, should be maximized. Members of the community where a business is located are also stakeholders in the business and have an interest in preserving jobs. The employees of the business itself are stakeholders and certainly wish to retain their jobs. A downsizing, or reduction in workforce, would offer the shareholders of the company a boost in earnings and share price. That same reduction, however, will affect the local economy and community in a negative way. Balancing the interests of these stakeholders is a standard used in resolving ethical dilemmas in business. Figure 3-1 lists the areas of concern that should be examined as businesses analyze an ethical dilemma.

As Figure 3-1 indicates, stakeholder analysis requires the decision maker to view a problem from different perspectives in the light of day. Stakeholder analysis requires measurement of the impact of a decision on various groups but also requires that public disclosure of that decision be defensible. The questions help the employee who is about to leave the office for half a day without taking vacation time: Could I tell my family or my supervisor that I have done this? These questions also help a company faced with the temptation of price fixing: Could I describe before a congressional committee what I am about to do?

In other situations, a business is not facing questions of dishonesty or unfair competition. In many ethical dilemmas, a business faces the question of taking voluntary action or simply complying with the law. Some experts maintain that the shareholders’ interest is paramount in resolving these conflicts among stakeholders. Others maintain that a business must assume some responsibility for social issues and their resolution. Economist Milton Friedman expresses his views on resolving the conflicts among stakeholders as follows:

A corporate executive’s responsibility is to make as much money for the shareholders as possible, as long as he operates within the rules of the game. When an executive decides to take action for reasons of social responsibility, he is taking money from someone else—from the stockholders, in the form of lower dividends; from the

Ethics in Government Employment

The state of Arizona mandates emissions testing for cars before drivers can obtain updated registrations. The emissions tests are conducted by a contractor hired by the state to operate the various emissions testing facilities around the state. In October 1999, the Arizona attorney general announced the arrest of 13 workers at one of the emissions testing facilities for allegedly taking payoffs of between $50 and $200 from car owners to pass their cars on the emissions tests when those cars fell below emissions standards and would not have been registered. Nearly half of the staff at the emissions facility were arrested.

Why is it a crime for someone working in a government-sponsored facility to accept a payment for a desired outcome? Is anyone really harmed by the payoffs to the workers?
**FIGURE 3-1  Guidelines for Analyzing a Contemplated Action**

1. Define the problem from the decision maker’s point of view.
2. Identify who could be injured by the contemplated action.
3. Define the problem from the opposing point of view.
4. Would you (as the decision maker) be willing to tell your family, your supervisor, your CEO, and the board of directors about the planned action?
5. Would you be willing to go before a community meeting, a congressional hearing, or a public forum to describe the action?
6. With full consideration of the facts and alternatives, reach a decision about whether the contemplated action should be taken.

In direct opposition to the Friedman view is the social responsibility view of Anita Roddick, CEO of Body Shop International. She has stated that she does not care about earning money because the sole reason for a business to exist is to solve social problems. In between these two views are compromise positions in which businesses exist primarily to benefit the shareholders but do take opportunities to solve social problems. Many businesses today have created flextime, job sharing, and telecommuting as work options for their employees to accommodate family needs. These options are a response to larger societal issues surrounding children and their care but may also serve as a way to retain a quality workforce that is more productive without the worry of poor child care arrangements. The law currently does not require businesses to furnish such options, but the businesses offer the programs voluntarily as a means of addressing a social issue.

In between the Friedman and Roddick views on business ethics and social responsibility are businesses with varying views on the role of business in society. Among these businesses are very profitable firms that are also involved in their communities through employees’ volunteer work and companies’ charitable donations. For example, Bill Gates, the CEO of Microsoft who is also ranked as the richest man in the United States, pledged, in 2003, $3 billion for fighting AIDS and providing childhood vaccine programs around the world. He has also used his foundation to provide scholarships for minorities. One different view on the social responsibility of business comes from Warren Buffett, the second richest man in the United States, according to the Forbes ranking, and the CEO of Berkshire Hathaway, a company with shares selling for more than $60,000 each. Mr. Buffett asks his shareholders whether they would like to donate to any charitable organization and then asks them to specify their charity of choice. Mr. Buffett’s view is that the shareholders, not he, should make decisions about corporate profits and their use. In 2002, the average amount for corporate charitable giving was 1.5 percent of pretax income.

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employees, in the form of lower wages; or from the consumer, in the form of higher prices. The responsibility of the corporate executive is to fulfill the terms of his contract. If he can’t do that in good conscience, then he should quit his job and find another way to do good. He has the right to promote what he regards as desirable moral objectives only with his own money.℠
Ethics and Social Responsibility

Ben & Jerry’s Homemade, Inc., is a Vermont-based ice-cream company founded by Ben Cohen and Jerry Greenfield, who began the company with the goal of social contribution. A portion of all proceeds from the sale of their ice cream is donated to charity.* The company issues strong position statements on social issues.

Following some slowing in market growth and reduction in profits, Cohen and Greenfield retired as officers of the company (although they remained majority shareholders and, therefore, in control of the board)** and hired Robert Holland as CEO. After Holland had been CEO for a year, a Japanese supplier approached him and offered to distribute Ben & Jerry’s ice cream in Japan. Holland turned down the offer because the Japanese company had no history of involvement in social issues and explained, “The only clear reason to take the opportunity was to make money.”

Do you agree with Holland’s decision? What approach do Ben & Jerry’s and Holland take with respect to their stakeholders? Is it troublesome that the company had not turned around financially when the offer was declined? Holland added that the only growth opportunities are in international markets. Is Ben & Jerry’s passing up business? Is this a good or bad practice for a company? Holland left the company shortly after the decision on the Japanese opportunity had been made. How do you view Holland’s position on business ethics and social responsibility? Is it best to find a company with values consistent with your own? How would you be able to tell the values of a company?

*Ben & Jerry’s gave 7.5 percent of its pretax income to charity.
**Ben & Jerry’s Homemade, Inc., has been sold and is now part of an international conglomerate, Unilever, Inc.

Ethics & the Law

Wal-Mart stores have banned three men’s magazines from sales in its stores. The banned magazines are *Maxim*, *Stuff*, and *FHM*. The magazines feature scantily clothed women and “bawdy humor.”

The banned products are parts of an ongoing series of decisions Wal-Mart has made about carrying products. Wal-Mart has long banned the sales of certain CDs in its stores. Last year it banned the sales of certain video games as well. Because it is the largest seller of CDs and DVDs, producers offer sanitized versions of these materials for sale at Wal-Mart.*

Why do you think Wal-Mart makes the voluntary decision to not sell certain products? Some argue that the First Amendment is violated with these bans on sales. Refer to Chapter 4 and evaluate whether they have a point.

Regardless of a firm’s views on social responsibility issues, the notions of compliance with the law and fairness in business transactions and operations are universal concerns. Values are an important part of business success. Business ethics is important for more than the simple justification that “it’s the right thing to do.” This section covers the significance of ethics in business success.

5. The Importance of Trust
Capitalism succeeds because of trust. Investors provide capital for a business because they believe the business will use it and return it with earnings. Customers are willing to purchase products and services from businesses because they believe the businesses will honor their commitments to deliver quality and then stand behind their product or service. Businesses are willing to purchase equipment and hire employees on the assumption that investors will continue to honor their commitment to furnish the necessary funds and will not withdraw their promises or funds. Business investment, growth, and sales are a circle of trust. Although courts provide remedies for breaches of agreements, no economy could grow if it were based solely on positive law and court-mandated performance. It is the reliance on promises, not the reliance on litigation, that produces good business relationships. In economics, the concept of rational expectations of investors and consumers plays a role in economic growth and performance. The assumption every investor makes is that his or her initial investment will earn a return. An assumption that employees make is that, absent problems with their performance, their employment will continue. Those assumptions encourage investment by investors and spending by employees. Their assumptions demonstrate trust in the relationship and in the underlying economic system.

As economists have had the opportunity to watch nations with new forms of government enter the international markets, they have documented distinctions in growth rates. In those countries where government officials control market access through individual payments to them, the business climate is stalled and growth lags behind that found in free-market nations.

Studies centering on a business’s commitment to values and its financial performance suggest that those with the strongest value systems survive and do so successfully. In the book *Built to Last* by James C. Collins and Jerry I. Porras, an in-depth look at companies with long-term growth and profits produced a common thread. That common thread was the companies’ commitment to values. All the firms studied had focused on high standards for product quality, employee welfare, and customer service.

A study of companies that had paid dividends for 100 years without interruption revealed the same pattern of values. Companies that had survived two world wars and a depression without missing a dividend remained committed to their customers and employees with standards of fairness and honesty.

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Coca-Cola has admitted that it paid a consultant $10,000 to drive up the demand for its Frozen Coke beverage being test-marketed in Burger Kings in the Richmond, Virginia, area. The consultant used the money to make donations to Boys and Girls Clubs. The clubs then provided meal coupons to the children in exchange for their doing their homework. The impressive demand that resulted from the Richmond area test market had Burger King investing $65 million to put the machines in restaurants around the country. However, the demand was not what it had been falsely alleged to be, and the result is that, following a six-week investigation by a law firm hired by the Coca-Cola board, Coca-Cola has admitted that the marketing studies were inflated.

The board investigation followed an allegation in a lawsuit filed by a former employee, Matthew Whitley. Whitley was terminated following his questioning of an expense claim by the consultant and his resulting investigation that produced an internal memo describing the consultant’s work on driving up the demand. Coca-Cola also issued an earnings restatement of $9 million based on an investigation of those allegations. The Wall Street Journal was following the Whitley lawsuit when the underlying issues emerged, and it reported the marketing scheme.* Coca-Cola settled with Burger King by paying $21 million.

Was this conduct ethical? Was it fraud? What does Mr. Whitley’s termination say about the company? Does he have protection? Why do you think the marketing managers decided to involve the consultant and report the false demand? What effect does this incident have on Burger King’s relationship with Coke?

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**ETHICS & THE LAW**

As you examine the following list of countries, those in the column labeled “Least Corrupt” (countries in which government officials are least likely to accept bribes) and those in the column marked “Most Corrupt” (countries in which government officials are most likely to accept bribes), can you comment on the business climates in them?

<table>
<thead>
<tr>
<th>Least Corrupt (Least Likely to Accept Bribes)</th>
<th>Most Corrupt (Most Likely to Accept Bribes)</th>
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<tbody>
<tr>
<td>Finland</td>
<td>Bangladesh</td>
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<td>Netherlands</td>
<td>Uganda</td>
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<tr>
<td>Denmark</td>
<td>Nigeria</td>
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<td>United Kingdom</td>
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<td>New Zealand</td>
<td>Paraguay</td>
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<td>Australia</td>
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<td>Norway</td>
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<td>Singapore</td>
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<td>Switzerland</td>
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<td>Hong Kong</td>
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<td>Canada</td>
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<td>Austria</td>
<td>Kazakhstan</td>
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<tr>
<td>Luxembourg</td>
<td>Azerbaijan</td>
</tr>
<tr>
<td>United States</td>
<td>Vietnam*</td>
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</table>

An examination of companies involved in an ethical breach demonstrates the impact of poor value choices on financial performance. A study of the impact of breaches of the law by companies showed that for five years after their regulatory or legal misstep, these companies were still struggling to recover the financial performances they had achieved prior to their legal difficulties.\textsuperscript{6}

After Enron announced that it would restate its income because it had been spinning off its debt obligations into off-the-book-entities, its share price dropped from $83 per share on January 14, 2001, to $0.67 per share on January 14, 2002.\textsuperscript{7} After WorldCom revealed that it had capitalized ordinary expenses, it had to reduce its earnings by $9 billion. The chief financial officers and other employees of both companies have been indicted. Their accounting firm, Arthur Andersen, was convicted of obstruction of justice and was forced to liquidate. Columbia Health Care’s share price dropped 58 percent and it experienced a 93 percent drop in earnings after it was charged with overbilling for Medicare reimbursements. Its share price dropped from $40 to $18. The nation’s largest hospital chain has had to spin off 100 hospitals and has paid record fines to settle the charges.\textsuperscript{8}

Ford and Firestone have faced everything from congressional hearings to public relations damage control as they have tried to answer questions about the Firestone Wilderness tires on the Ford Explorer. Because of a series of accidents involving the Explorers with these tires, litigation began a spiral of events that has left both companies trying to determine what has happened and whether they could have acted sooner in recalling the tires in the United States following recalls in other countries.\textsuperscript{9}

Asbestos liability bankrupted Johns-Manville when documentation showed that the company’s executives knew about the lethal effect of asbestos on the lungs but took no action to warn buyers and users of the product. Bausch & Lomb, Leslie Fay, Phar-Mor, Cendant, Sunbeam, Xerox, and even General Electric all experienced financial fallout after accounting irregularities carried out by company officers, assisted by many employees, or earnings restatements were issued following the application of accounting rules. Martha Stewart, a billionaire, has been charged with federal crimes related to her conduct after she sold her ImClone stock one day prior to the FDA’s announcement that it was not yet approving the drug for the market. ImClone is a bio-tech company that was headed by Ms. Stewart’s friend, former CEO Sam Waksal, who entered a plea regarding his activities related to the sales of his shares in advance of the FDA announcement and is now serving time. As a result, Ms. Stewart’s own company, Omnimedia, International, which was not involved in the ImClone share trading and does not face any charges of earnings misstatements, has still seen a dramatic drop in earnings and stock prices because of the concerns about Ms. Stewart and shareholder concerns about their ability to trust her. Bankruptcy and/or free falls in the worth of shares are the fates that await firms that make poor ethical choices. Often even the conduct of their CEOs affects the value of the company and its shares.

\textsuperscript{6}Melinda S. Baucus and David A. Baucus, “Paying the Piper: An Empirical Examination of Longer-Term Financial Consequences of Illegal Corporate Behavior,” 40 Academic Management Journal 129 (1997).
\textsuperscript{7}From stock price chart, http://www.enron.com.
\textsuperscript{9}Alex Taylor, “Jacques Nasser’s Biggest Test,” Fortune, September 18, 2000, 123.
7. The Importance of a Good Reputation

Richard Teerlink, the CEO of Harley-Davidson, once said, “A reputation, good or bad, is tough to shake. A breach of ethics is costly to a firm not only in the financial sense of drops in earnings and possible fines. A breach of ethics often carries with it a lasting memory that affects the business and its sales for years to come. For Example, following Sears, Roebuck’s settlement with the California Consumer Affairs Department of fraud charges involving the operation of its auto centers, Montgomery Ward Auto Centers enjoyed an increase in business. Customers were concerned about taking their cars to Sears because of the scandal surrounding the nationally reported charges of unnecessary repairs. Because business declined, Sears was forced to close some of its auto centers.

When an ethical breach occurs, businesses lose that component of trust important to customers’ decisions to buy and invest. For Example, Beech-Nut, the baby food company, has an outstanding product line and offers quality at a good price. Yet it has not regained its former market share as a result of the federal charges it faced in 1986. Its apple juice tasted good, but it was a chemical concoction containing no apple juice despite advertising claims to the contrary. Even though no one was harmed, the customers’ view of Beech-Nut changed. Trust disappeared, and so did a good portion of the company’s market share. Almost two decades later, the company continues to struggle to overcome that one-time breach in ethics.

8. Business Ethics and Business Regulation: Public Policy, Law, and Ethics

When business behavior results in complaints from employees, investors, or customers, laws or regulations are often used to change the behavior. For Example, the bankruptcy of Orange County and the large losses experienced by Procter & Gamble and Gibson Greetings resulting from their heavy investments in high-risk financial instruments motivated the Securities and Exchange Commission (SEC) (see Chapter 46) to promulgate regulations about disclosures in financial statements on high-risk investments known as derivatives. The Federal Reserve stepped in to regulate virtually all aspects of credit transactions, focusing on the disclosure of the actual costs of credit to ensure full information for borrowers. Confusion among consumers about car leasing and its true costs and the fees applicable at the end of the lease terms caused the Federal Reserve to expand its regulation of credit to car leases. Figure 3-2 depicts the relationships among ethics, the social forces of customers and investors, and the laws that are passed to remedy the problems raised as part of the social forces movement.

From the nutrition facts that appear on food packages to the type of pump at the gas station, government regulation of business activity is evident. Congress begins its legislative role and administrative agencies begin their process of regulation (see Chapter 6) when congressional hearings and studies reveal abuses and problems within an industry or throughout business. Legislation and regulation are responses to

activities of businesses that are perfectly legal but raise questions of fairness that cause customer and investor protests.

Antidiscrimination laws were passed when evidence established that many companies had policies that required, for example, pregnant employees to stop working. Hotels at one time had policies that permitted minorities to work in kitchens and perform housekeeping tasks but did not permit them to hold “guest-contact” positions. These policies did not violate any laws at the time. However, employees justifiably raised concerns about the fairness or the ethics of such policies, and legislation was passed, in large part because of the unwillingness of business to change its practices, to remedy employees’ concerns. Businesses that act voluntarily on the basis of value choices often avoid the costs and the sometimes arbitrariness of legislation and regulation. Voluntary change by businesses is less costly and is considered less intrusive. Regulation costs are substantial, and regulation is extensive.

Businesses that respond to social forces and the movements of the cycle of societal interaction gain a competitive advantage. Businesses that act irresponsibly and disregard society’s views and desire for change will speed the transition from value choice to enforceable law. Businesses should watch the cycle of social forces and follow trends there to understand the values attached to certain activities and responses. These values motivate change either in the form of voluntary business activity or legislation. All values that precipitate change have one of several basic underlying goals. These underlying goals, discussed in the following sections, offer signals about the pattern of social change.

(a) **Protection of the State** A number of laws exist today because of the underlying goal or value of protection of the state. Laws that condemn treason are examples of laws passed to preserve the government of the state. Another less dramatic set of laws offering protection to the state are the tax codes, which provide authority for collecting taxes for the operation of government facilities and enforcement agencies. The Patriot Act and airport security regulations are also examples of government programs and regulations created with the protection and security of the state as the goal.
(b) Protection of the Person A second social force is protection of the person. From the earliest times, laws were developed to protect the individual from being injured or killed. Criminal laws are devoted to protection of individuals and their properties. In addition, civil suits permit private remedies for wrongful acts toward people and their property. Over time, the protection of personal rights has expanded to include the rights of privacy and the protection of individuals from defamation. Contract rights are protected from interference by others. Laws continue to evolve to protect the reputations, privacy, and mental and physical well-being of individuals.

Individual rights have been the values at the core of legislation and regulation relating to governmental assistance programs, public schools, service on a jury, and access to public facilities. The antidiscrimination laws that affect nearly all businesses are grounded in the value of protection of the individual. Labor laws and regulations exist to protect the individual rights of workers.

(c) Protection of Public Health, Safety, and Morals The food-labeling regulations discussed earlier are an example of laws grounded in the value of protecting the safety and health of individuals. Food and restaurant inspections, mandatory inoculation, speed limits on roadways, mandatory smoke detectors and sprinkler systems in hotels, and prohibitions on the sale of alcohol to minors are all examples of laws based on the value of safety for the public. Zoning laws that prohibit the operation of adult bookstores and movie theaters near schools and churches are examples of laws based on moral values.

(d) Protection of Property: Its Use and Title Someone who steals another’s automobile is a thief and is punished by law with fines and/or imprisonment. A zoning law that prohibits the operation of a steel mill in a residential area also provides protection for property. A civil suit brought to recover royalties lost because of another’s infringement of one’s copyrighted materials is based on federal laws that afford protection for property rights in nontangible or intellectual property (see Chapter 10). Laws afford protection of title for all forms of property. The deed recorded in the land record is the legal mechanism for protecting the owner’s title. The copyright on a software program or a song protects the creator’s rights in that intellectual property. The title documents issued by a department of motor vehicles afford protection of title for the owner of a car.

Those who have title to property are generally free to use the property in any manner they see fit. However, even ownership has restrictions imposed by law. A landowner cannot engage in activities on his or her property that damage another’s land or interfere with another’s use of land. A business may operate a factory on its real property, but if the factory creates a great deal of noise, adjoining landowners may successfully establish it as a nuisance (see Chapter 49) that interferes with their use and enjoyment of their land. The law affords remedies for such a nuisance that might include an injunction, or court order, limiting the hours of the factory’s operation so that neighbors have the opportunity to sleep.

If that factory releases chemicals into the river flowing nearby, others’ rights and use of their land are affected. Environmental laws (see Chapter 50) have been passed that regulate the use of property. Those environmental laws evolved through social activism after landowners and residents located near factories and other operations with harmful emissions became concerned about the impact on the value of their properties as well as the impact on their health and safety. Environmental laws thus emerged as regulation of land use in response to concerns about legal, but harmful, emissions by companies.
**Protection of Personal Rights** The desire for individual freedom to practice religion and freedom from political domination gave rise to the colonization of the United States and, eventually, the American Revolution. The desire for freedom from economic domination resulted in the free enterprise philosophy that exists in the United States today. Individual freedoms and personal rights continue as a focus of value discussions followed by legislation if those individual rights are violated.

Economic freedoms and the free enterprise system were in jeopardy at the end of the nineteenth century as large conglomerates began to dominate certain markets and inhibit the ability of individuals to compete. Repressive activities in the marketplace by some companies led to federal regulation in the form of antitrust laws. These laws were passed in response to social concerns about economic freedom and individual opportunities within the economy (see Chapter 5). For example, Microsoft’s 90 percent domination of the operating systems market led to extensive antitrust litigation against the company that was eventually settled.

**Enforcement of Individual Intent** When someone has voluntarily entered into a transaction, there is a responsibility to carry forward the promises made. Principles of honesty and honoring commitments are the ethical values at the heart of the parties’ conduct in carrying out contracts. If, however, the parties do not keep their promises, the law does enforce transactions through sets of rules governing requirements for them. For Example, if a person provides by will for the distribution of property at death, the law will generally allow the property to pass to the persons intended by the deceased owner. The law will also carry out the intentions of the parties to a business transaction.

Laws exist to honor the intent of parties because not all commitments are fulfilled voluntarily. The law may impose requirements that a transaction or agreement be in writing to ensure that the intent of the parties is adequately documented and fulfilled (see Chapter 17). The law may also place restrictions on honoring intentions. A contract to commit a murder may be evidenced by intent and fully documented in writing. However, the intent of the parties will not be honored because of the social values manifested in the protection of individuals and individuals’ rights and safety.

**Protection from Exploitation, Fraud, and Oppression** Many laws have evolved because businesses took advantage of another group. Some groups or individuals have been given protection by the law because of excesses by businesses in dealing with them. Minors, or persons under legal age (see Chapter 14), are given special protections under contract laws that permit them to disaffirm their contracts so they are not disadvantaged by excessive commitments without the benefit of the wisdom of age and with the oppressive presence of an adult party.

The federal laws on disclosure with respect to the sales of securities and shareholder relations (see Chapters 45 and 46) were developed following the 1929 stock market crash when many investors lost all they had because of the lack of candor and information by the businesses in which they were investing.

Food manufacturers have exclusive control over the canning and processing of their products. The opportunity for taking advantage of customers who do not generally have access to the factories and plants is great. The contents of canned products are not visible to consumers before they make their purchases. Because of excesses and exploitations by food processors, there are both federal and state regulations of food processing and food labeling. Adulteration or poisoning of food products carries criminal penalties. Misrepresenting the contents in food packages may constitute a federal felony.
(h) Furtherance of Trade  Some laws are the result of social forces seeking to simplify business and trade. Installment sales and credit transactions, and their accompanying laws and regulations, have made additional capital available for businesses and provided consumers with alternatives to cash purchases. The laws on checks, drafts, and notes have created instruments used to facilitate trade. The Federal Reserve System’s Board of Governors and its oversight of federal banks and interest rates have mitigated the harmful effects of alternating economic periods of depression and inflation.

(i) Protection of Creditors and Rehabilitation of Debtors  Society seeks to protect the rights of creditors and to protect them from dishonest or fraudulent acts of debtors. Initially, creditors are protected by the laws that make contracts binding and enforceable. Creditors are also protected by statutes that make it a fraud for a debtor to conceal property from a creditor. To meet the social demands for facilitation of trade, credit transactions were authorized. With that authorization, however, came the demand for the creditor’s assurance of repayment by the debtor. Mortgages, security interests, and surety relationships (see Chapters 32, 34, and 49) are mechanisms created by law to provide creditors with legal mechanisms for collecting their obligations.

When collection techniques became excessive and exploitative, new laws on debtors’ rights were enacted. Debtors’ prisons were abolished. Disclosure requirements for credit contracts were mandated by Congress. Collection techniques were limited through the Fair Debt Collections Practices Act (see Chapter 33). The remedy of bankruptcy was afforded debtors under federal law to provide them with an opportunity to begin a new economic life when their existing debts reached an excessive level and could no longer be paid in a timely fashion (see Chapter 35).

(j) Stability and Flexibility  Stability is particularly important in business transactions. When you buy a house, for example, you not only want to know the exact meaning of the transaction under today’s law, but you also want the transaction to have the same meaning in the future.

Because of the desire for stability, courts will ordinarily follow former decisions unless there is a strong reason to depart from them. Similarly, when no former case bears on the point involved, a court will try to reach a decision that is a logical extension of some former decision or that follows a former decision by analogy rather than strike out on a new path to reach a decision unrelated to the past.

If stability were always required, the cause of justice would often be defeated. The reason that originally existed for a rule of law may have ceased to exist. Also, a rule may later appear unjust because it reflects a concept of justice that is outmoded or obsolete. The policies surrounding adoption of children and the rights of natural versus adoptive parents have continued to evolve because of changing attitudes about these relationships and new technology that permits laboratory creation and insemination.

The typical modern statute, particularly in the area of business regulation, often contains an escape clause by which a person can “escape” from the operation of the statute under certain circumstances.  For Example, a rent control law may impose a rent ceiling, that is, a maximum rent a landlord can charge a tenant. The same law may also authorize a greater charge when special circumstances make it just to allow such an exception. For example, the landlord may have made expensive repairs to the property or taxes on the property may have increased substantially.

Protection of the person is frequently the controlling factor in determining whether a court should adhere to the common law, thereby furthering stability, or whether it should change the law, thereby furthering flexibility.
Case Summary

The One-Click Warranty Waiver

Facts: Mortenson Company, Inc., a contractor, upgraded its version of Timberline Software’s Bid Analysis Software, which is used by contractors in preparing construction bids. When the software arrived at Mortenson, employees unpacked and activated it. Mortenson employees did not notice that a license agreement is printed on the outside of each sealed envelope containing the diskettes. The license agreement instructs the buyer to read the terms “before using the programs. Use of the programs indicates your acknowledgement that you have read this license, understand it, and agree to be bound by its terms and conditions.” The terms also provided that “[i]f you do not agree to these terms and conditions, promptly return the programs and user manuals to the place of purchase and your purchase price will be refunded.” The terms limited Timberline’s liability for any errors caused by the software programs to a reimbursement for the license fee. Buyers could not recover either compensatory or consequential damages.

After using the Timberline software and submitting a bid, Mortenson discovered a $2 million error and sought to recover damages from Timberline for being forced to perform on the contract for which it had accidentally submitted the incorrect and low bid of $2 million. Timberline defended on the grounds of its warranty limitation placed in the packaging of its software. The trial court granted summary judgment for Timberline, and Mortenson appealed.

Decision: Although the case circumstances involve the new technology of computers and software, the issue remains one of basic contract law: Are buyers bound by terms on the boxes, labels, and packaging of the products they buy? Is “buy now, terms later” enforceable against buyers of software? Noting the practical issues in contracting in the technology age (contracts are entered into over the phone and the Internet), the court held that the terms were enforceable as long as they were not unconscionable. Terms are unconscionable when the buyer would have no reason to know that the terms were there (i.e., the terms were inconspicuous) or when the terms depart substantially from industry custom.

In this case, the terms on the box were relatively common for the industry, and the buyer was probably aware anyway that the liability limitation existed, as it does for most software products. Although Mortenson and Timberline did not specifically negotiate the limitations-of-remedies clause, this one factor is not conclusive. The introductory screen warned that use of the program was subject to a license. This warning placed Mortenson on notice that use of the software was governed by a license. Mortenson had reasonable opportunity to learn and understand the terms of the agreement. The limitations provision was not hidden in a maze of fine print but appeared in all capital letters. [Mortenson Co., Inc. v Timberline Software Corp., 970 P2d 803 (Wash 1999)]

C. How to Recognize and Resolve Ethical Dilemmas

Business managers find themselves in circumstances in which they are unclear about right and wrong and are confused about how to resolve the dilemmas they face. A recent survey showed that 98 percent of all Fortune 500 companies have codes of ethics designed to help their employees recognize and resolve ethical dilemmas. Nearly 65 percent of those firms provide their employees with some form of training in ethics. These codes of ethics provide employees with information about categories of behavior that constitute ethical breaches. Regardless of the industry, the type of busi-

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ness, or the size of the company, certain universal categories can help managers recognize ethical dilemmas. Figure 3-3 provides a list of those categories.

9. Categories of Ethical Behavior

(a) Integrity and Truthfulness  Mark Twain once wrote, “Always tell the truth. That way you don’t have to remember anything.” As discussed earlier, trust is a key component of business relationships and of the free enterprise system. Trust begins with the belief that honesty is at the heart of relationships. Many contract remedies in law are based on the failure of the parties to be truthful with each other. If you purchase a home that has been certified as termite-free and you then discover termites in the home shortly after you move in, someone has not been truthful. If you also discover that two termite inspections were conducted and that the first one, which revealed there were termites, was concealed from you, your trust in both the sellers and their exterminators is diminished.

An assurance that a seller has the expertise to handle your project is important in building that relationship. If you discover later that the seller lacks the expertise, you are harmed by the delay and possible poor work that has been done. When the prospectus for a stock offering fails to provide full information about the company’s obsolete inventory, investors are not given the full truth and are harmed when they invest without complete disclosure. Investors become skeptical when offerings do not carry with them a very basic level of honesty in their disclosures. Honesty is necessary for the wheels of commerce to turn.

Integrity is the adherence to one’s values and principles despite the costs and consequences. For Example, an executive contracted with a variety of companies to sell his hard-to-find computer components. When he was approached by one of his largest customers to break a contract with a small customer, the executive refused. The customer assured the executive it would be his last order with the company if he did not get more components. Despite facing the threat of losing a multimillion-dollar customer, the executive fulfilled his promises to the small purchasers. The executive kept his word on all of his contracts and demonstrated integrity.

(b) Promise Keeping If we examine the types of things we do in a day, most are based on promises. We promise to deliver goods either with or without a contract. We promise to pay the dentist for our dental work. We promise to provide someone with a ride. Keeping those promises, regardless of whether there is a legal obligation to do so, is a key component of being an ethical person and practicing ethical business. Keeping promises is also evidence of integrity.

FIGURE 3-3 Categories of Ethical Behavior

1. Integrity and truthfulness
2. Promise keeping
3. Loyalty—avoiding conflicts of interest
4. Fairness
5. Doing no harm
6. Maintaining confidentiality
The issue of employee downsizing is debated with the underlying question of whether the downsized employees had a promise from their company of continued employment. As stakeholder analysis is reviewed, the ethical issue surrounding the question is whether there are promises to others who are at risk. Weren't shareholders promised a return on their investment? Weren't suppliers promised payment? In many circumstances, the question is not whether a promise will be kept but rather which promise will be kept. The strategic issue is whether businesses should make commitments and promises in circumstances that create a very thin margin of profit and perhaps even thinner margin for error. Over the long term, the importance of a company's keeping its promises to all stakeholders translates into the reputation of the business.

(c) Loyalty—Avoiding Conflicts of Interest

An employee who works for a company owes his or her allegiance to that company. Conduct that compromises that loyalty is a conflict of interest. For Example, suppose that your sister operates her own catering business. Your company is seeking a caterer for its monthly management meetings. You are responsible for these meetings and could hire your sister to handle the lunches furnished at the meetings. Your sister would have a substantial contract, and your problems with meal logistics would be solved. Nearly all companies have a provision in their code of ethics covering this situation. An employee cannot hire a relative, friend, or even his or her own company without special permission because it is a conflict of interest. Your loyalty to your sister conflicts with the loyalty to your employer, which requires you to make the best decision at the best price.

A conflict of interest arises when a purchasing agent accepts gifts from suppliers, vendors, or manufacturers' representatives. The purchasing agent has introduced into the buy-sell relationship an element of quid pro quo, or the supplier's expectation that the gift will enjoy a return from the agent in the form of a contract. Some companies have zero tolerance for conflicts and establish a complete prohibition on employees...
ETHICS & THE LAW

The University of California at Berkeley has implemented a new step in its admission process. The Haas School of Business has begun running background checks on students who have applied to determine whether the information in their applications is correct. The Wharton School implemented a similar procedure and charges applicants a $35 fee for these background checks.

Of the 100 students admitted to Berkeley in the fall of 2003, 5 students were found to have offered false information on their admissions applications. The most common type of false information was the job titles they held, and the second most common type was their number of years of work experience. Haas admissions officers indicated that had the students not lied, they otherwise met the GMAT score and GPA standards for admission to Haas.

What risk do the students take in lying on their applications? What are the long-term consequences?


accepting any gifts from suppliers and manufacturers. For Example, Wal-Mart buyers are not permitted to accept even a cup of coffee from potential merchandise suppliers, and Amgen’s buyers can go out to dinner with a supplier only if Amgen pays.

(d) Fairness In business transactions in which the buyer was not told about the crack in the engine block or the dry well on the property, a typical response is “That’s not fair. I wouldn’t have bought it if I’d known.” A question often posed to the buyer in response is “Wouldn’t you have done the same thing?” We feel differently about such situations, depending on whether we are the victims of unfairness or whether we hold the superior knowledge in the transaction. The ethical standard of fairness requires both sides to ask these questions: “How would I want to be treated? Would this information make a difference to me?” Imposing our own standards and expectations on our own behavior in business transactions produces fairness in business.

(e) Doing No Harm Imagine selling a product that your company’s internal research shows presents significant health dangers to its users. Selling the product without disclosure of the information is unfair. But there is the additional ethical breach of physical harm to your customers and users. Ford designed and sold its Pinto with a fundamental flaw in the placement of the car’s gas tank. Rear-end collisions in which a Pinto was involved resulted, even at very low speeds, in fires that engulfed the car so quickly that occupants could not always escape from it. An internal memo from engineers at Ford revealed that employees had considered doing an analysis of the risk of the tanks versus the cost of redesign, but never did. Peter Drucker’s advice on ethics for businesses is *primum non nocere*, or “above all, do no harm.”

(f) Maintaining Confidentiality Often the success of a business depends on information or technology that it holds. If the competitive edge that comes from the business’s peculiar niche or knowledge is lost through disclosure, so also are profits. Employees not only owe a duty of loyalty to their employers, but they also owe an obligation of confidentiality. Employees should not use, either personally or through a competitor, information they have obtained through their employer’s work or research. Providing customer lists or leads is a breach of employees’ obligation of confidentiality.
Richard N. Perle served as chairman of the Defense Policy Board, a position appointed by the Secretary of Defense, Donald H. Rumsfeld. Mr. Perle was hired by Global Crossing, a telecommunications company in Chapter 11 bankruptcy, to work with the Defense Department because the Department opposed the sale of Global Crossing to Hutchison Whampoa and Singapore Technology, two foreign companies. Mr. Perle earned $725,000 for his work, $600,000 of which was due if the Defense Department approved the sale. The Defense Department opposed the sale because it used the Global Crossing fiber-optics network for its telecommunications needs and the sale would put that network under Chinese control.

Mr. Perle filed an affidavit in the review process for the FBI and Defense Department (whose approvals were required) that contained the following language:

As the chairman of the Defense Policy Board, I have a unique perspective on and intimate knowledge of the national defense and security issues that will be raised by the CFIUS review process that is not and could not be available to the other CFIUS professionals. [CFUIS is the Committee on Foreign Investment in the United States and consists of representatives from the Defense Department and other agencies. CFIUS has the authority to block foreign acquisitions.]*

When asked about his dual role, Mr. Perle said,

I've abided by the rules. The question, I think, is have I recommended anything to the secretary or discussed this with the secretary, and I haven't. The alternative is if you are on the board, you can't have any action before the Defense Department. That isn't the rule. If that were the rule, I'd have to make a choice between being on an unpaid advisory board and my business.**

What ethical issue exists in Mr. Perle's conduct?


**Id. at C2.

In addition, managers have responsibilities regarding their employees’ privacy. Performance evaluations of individual employees are private and should never be disclosed or revealed, even in one-on-one conversations outside the lines of authority and the workplace.

10. Resolving Ethical Dilemmas

Recognizing an ethical dilemma is perhaps the easiest part of business ethics. Resolution of that dilemma is more difficult. The earlier section on stakeholders offers one model for resolution of ethical dilemmas (see Figure 3-1). Other models have been developed to provide managers with methods of analysis for resolving dilemmas in a timely fashion.

(a) Blanchard and Peale Three-Part Test Dr. Kenneth Blanchard, author of books on the One-Minute Manager, and the late Dr. Norman Vincent Peale developed a model for evaluating ethical breaches that is widely used among Fortune 500 compa-
ETHICS & THE LAW

Ethics and Fairness

Dateline NBC, a television newsmagazine program that airs several nights a week, presented a segment on General Motors (GM) and the safety of GM’s trucks with sidesaddle gas tanks. Dateline producers staged and taped an accident with a GM truck that showed a gas tank explosion and subsequent fire that engulfed the pickup truck. The tape was shown on Dateline. Disclosures of several crew members later revealed that explosive devices had been used to create the scene for the cameras, but the use of those devices was not disclosed during the Dateline piece.*

Was it fair to use the explosive devices? Was it fair to use the explosive devices and not disclose that to the audience? Was the program fair to GM?

Note: Dateline later read an on-air apology for using the tape.

(b) The Front-Page-of-the-Newspaper Test This simple but effective model for ethical evaluation helps a manager visualize the public disclosure of proposed conduct. When he took over Salomon Brothers after its bond-trading controversy, Warren Buffett described the newspaper test as follows:

Contemplating any business act, an employee should ask himself whether he would be willing to see it immediately described by an informed and critical reporter on the front page of his local paper, there to be read by his spouse, children, and friends. At Salomon, we simply want no part of any activities that pass legal tests but that we, as citizens, would find offensive.16

(c) Laura Nash Model In her work, business ethicist Laura Nash has developed a series of questions to help businesspeople reach the right decision in ethical dilemmas. Her questions are: Have you defined the problem accurately? How would you define

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ETHICS & THE LAW

The cover of *Fortune* magazine from May 14, 2001, featured a picture of Wall Street financial analyst Mary Meeker and the words, “Can we ever trust again?”* The inside story focused on the relationship of underwriters, analysts, and brokerage houses with the companies whose stocks they were touting and selling. They had continued to pump the virtues of stock shares they knew had overinflated prices. When the market bubble burst, the losses to shareholders were catastrophic. The analysts, underwriters, and brokers did not violate the law. Those in the financial markets had too much at stake to be honest with investors.

During 2002, new stories about analysts emerged, such as that of Jack Grubman, the analyst for Salomon Smith Barney who continued to tout WorldCom stock even as it was headed downward and into financial ruin.** Jack Grubman was the father of twins, and he wanted to see them admitted to one of Manhattan's most prestigious preschools—the 92nd Street Y. Mr. Grubman wrote a memo to Sanford Weill, the chairman of Citigroup, that contained the following language:

> On another matter, as I alluded to you the other day, we are going through the ridiculous but necessary process of pre-school applications in Manhattan. For someone who grew up in a household with a father making $8,000 a year and for someone who attended public schools, I do find this process a bit strange, but there are no bounds for what you do for your children.

> Anything, anything you could do Sandy would be greatly appreciated. As I mentioned, I will keep you posted on the progress with AT&T which I think is going well.

> Thank you.

Citigroup pledged $1 million to the school at about the same time Grubman's children were admitted. Mr. Weill, Mr. Grubman's CEO, asked Mr. Grubman to “take a fresh look” at AT&T, a major corporate client of Citigroup. Mr. Weill served on the board of AT&T, and AT&T's CEO, C. Michael Armstrong, served as a Citigroup director. Mr. Weill was courting Armstrong's vote for the ouster of his cochairman at Citigroup, John Reed. A follow-up e-mail from Mr. Grubman to Carol Cutler, another New York analyst, connected the dots:

> I used Sandy to get my kids in the 92nd Street Y pre-school (which is harder than Harvard) and Sandy needed Armstrong's vote on our board to nuke Reed in showdown. Once the coast was clear for both of us (ie Sandy clear victor and my kids confirmed) I went back to my normal self on AT&T.

At the same time as all the other movements, Mr. Grubman upgraded AT&T from a “hold” to a “strong buy.” After Mr. Reed was ousted, Mr. Grubman downgraded AT&T again. Mr. Grubman said that he sent the e-mail “in an effort to inflate my professional importance.” In another e-mail, Mr. Grubman wrote, “I have always viewed [AT&T] as a business deal between me and Sandy.”

The *Fortune* headline on June 10, 2002, read, “In search of THE LAST HONEST ANALYST.”***

Were there conflicts of interest in this situation? Do you think any laws were violated? How do you think such problems in the market will be fixed? What types of rules do you think will result? Why?

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*“Can We Ever Trust Again?” *Fortune*, May 14, 2000 (cover).
***“In search of THE LAST HONEST ANALYST,” *Fortune*, June 10, 2002 (cover).
the problem if you stood on the other side of the fence? How did this situation occur in
the first place? What is your intention in making this decision? How does the intention
compare with the probable results? Whom could your decision or action injure? Can
you discuss your decision with the affected parties? Are you confident that your posi-
tion will be as valid over a long period of time as it seems now? Could you discuss your
decision with your supervisor, coworkers, officers, board, friends, and family?

The Nash model requires an examination of the dilemma from all perspectives.
Defining the problem and how the problem arose provides the business with assistance

**ETHICS & THE LAW**

*Ethics and Lying to Get Ahead*

A study by an executive search firm revealed that 25 percent of all the résumés they
reviewed contained inaccurate information about the individual’s educational back-
ground or past employment. The types of inaccuracies included listing attendance
at and the receipt of a degree from a university that the applicant never attended
and misrepresenting responsibilities at previous jobs (e.g., a sales manager referring
to himself on his résumé as “director of marketing”).

Another study by Rutgers University concluded, based on surveys conducted of
students, that 75 percent of all students in master of business administration
(MBA) programs lied or cheated to get into their graduate programs. Examples of
their misconduct included cheating in undergraduate school, falsifying letters of
reference, and having someone else take the Graduate Management Admission Test
(GMAT) for them.

Ronald L. Zarrella, the CEO of Bausch & Lomb, admitted that he had
included false information in his résumé. His résumé stated that he had an MBA
from New York University (NYU). He had attended NYU and taken graduate
courses in business at night while he was working for Bristol-Myers, but he never
completed the degree program. The information from the résumé had been
included in Bausch & Lomb press releases since 1982. In addition, CSFB released
a statement indicating that information on Mr. Zarrella regarding his serving on its
subsidiary’s board, First USA, was inaccurate. Mr. Zarrella instead served on the
board of “US First,” a nonprofit organization that supported students entering the
sciences and engineering fields.

The news about this false information resulted in a drop of $1.01 in the price
of Bausch & Lomb’s shares from $31.48. Mr. Zarrella said he would not resign, and
the Board issued a statement expressing confidence in him. Mr. Zarrella had been
hired as CEO just 11 months before this incident. Bausch & Lomb had hired
Heidrick & Struggles to conduct its CEO search at that time, and the company
had not checked Mr. Zarrella’s background because he came in as a candidate
through a board member’s recommendation and not through the search firm.

Why do people lie about their backgrounds and qualifications? Is anyone really
hurt by this individual misconduct? Why is it important that the information on
résumés and applications for graduate school be accurate?

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**Carol Innerst, “Colleges Are Stepping Up the War Against Cheaters,” *Washington Times*, November 6–12, 1995, 25.
in avoiding the dilemma again. For Example, suppose that a supervisor is asked to provide a reference for a friend who works for her. The supervisor is hesitant because the friend has not been a very good employee. The ethical dilemma the manager believes she faces is whether to lie or tell the truth about the employee. The real ethical dilemma is why the supervisor never provided evaluation or feedback indicating the friend’s poor performance. Avoiding the problem in the future is possible through candid evaluations. Resolving the problem requires that the supervisor talk to her friend now about the issue of performance and the problem with serving as a reference.

One final aspect of the Nash model that businesspeople find helpful is a question that asks for a perspective on an issue from family and friends. The problem of group-think in business situations is very real. As businesspeople sit together in a room and discuss an ethical dilemma, they can persuade each other to think the same way. The power of consensus can overwhelm each person’s concerns and values. There is a certain fear in bringing up a different point of view in a business meeting. Proper perspective is often lost as the discussion centers around numbers. Therefore, bringing in the views of an outsider is often helpful. For example, when McNeil, the manufacturer of Tylenol, was faced with the cyanide poisonings from contaminated capsules sold in the Chicago area, the decision about existing inventory had to be made. It was clear to both insiders and outsiders that the poison had not been put in the capsules at McNeil but, rather, after delivery to the stores. Despite the huge numbers involved in the recall and destruction of inventory, the McNeil managers made the decision easily because they viewed the risk to their own families, that is, from the outside. From this standpoint, it became a question of life, and not a question of numbers.

ETHICS & THE LAW

Bribery and Ethics

Salt Lake City, Utah, had been a contender as a potential site for the Winter Olympics for 30 years. Each time, the city, famous for its extensive ski resorts and powder snow, lost to other cities around the world. When city and state officials and representatives from business made their bid for the 2002 Winter Olympics, they were determined to win. During the course of the International Olympic Committee’s decision-making process, some members of the Salt Lake City Olympic Committee gave benefits to members of the International Olympic Committee. Those benefits included everything from entertainment to medical care and college educations for family members of International Olympic Committee members.

When all of the perks were revealed, members of the International Olympic Committee, as well as the Salt Lake City Olympic Committee, resigned. Some Olympic sponsors withdrew.*

How could the Blanchard and Peale test have helped those involved in courting the International Olympic Committee? Does it matter that those kinds of benefits and perks are expected in the cultures of some of the International Olympic Committee members?

ETHICS & THE LAW

Ethics and Downsizing

Aaron Feuerstein is the owner of Malden Mills, a textile plant in Methuen, Massachusetts. The company was founded by Feuerstein’s grandfather in 1906 as a swim-suit and sweater manufacturer. Feuerstein changed the direction of traditional garment manufacturing when he switched the factory to Polartec production. Polartec is a revolutionary fabric made from recycled plastic bottles and is used in skiing and hiking clothing because of its unique qualities: warm, lightweight, and easy to dry and dye. L.L. Bean, Patagonia, and Eddie Bauer are all on Malden Mills’ customer list, which has generated $425 million in sales each year.

On December 11, 1995, the Malden Mills factory was almost completely destroyed by a fire started by a boiler that exploded. Feuerstein held a meeting with his employees several days later and guaranteed their pay for 30 days and their health benefits for 90 days. Malden Mills had 3,000 employees and an annual payroll of $65 million.

Feuerstein gave all of his employees three months’ pay and had all but 20 percent working full-time again by March 1996. By midsummer 1996, Malden Mills was back at full production. One employee said, “Another person would have taken the insurance money and walked away. I might have done that.”

Feuerstein described his role as follows:

*The fundamental difference is that I consider our workers an asset, not an expense. I have a responsibility to the worker, both blue-collar and white-collar. I have an equal responsibility to the community. It would have been unconscionable to put 3,000 people on the streets and deliver a death blow to the cities of Lawrence and Methuen. Maybe on paper our company is worth less to Wall Street, but I can tell you it’s worth more. We’re doing fine.***

Was it right for Feuerstein to keep his promise to employees? Did he really have a promise to keep? Does it matter that Malden Mills was not a publicly held company? In 2002, Malden Mills entered Chapter 11 bankruptcy. Do you think it was too ethical to be financially successful?

**id.
***Id.

(d) Wall Street Journal Model The Wall Street Journal presented a simple, three-prong test for resolving ethical dilemmas known as the three-C model: (1) Will this conduct be in compliance with the law? (2) What contribution does this decision make to the shareholders? To the community? To the employees? (3) What are the consequences of this decision? This model requires an examination of the impact of a choice, which then produces a different perspective on a course of conduct. For Example, Sears paid $475 million in fines and penalties for its unauthorized collection of debts from debtors who were in bankruptcy or had debts discharged in bankruptcy. Such collection beyond what the law allows was not in compliance with the law.18 The contribution to the company was more collections and hence more cash, but the consequences were the large fine and the damage to Sears’ reputation for putting its

interests above the law and above the interests of other creditors who conducted themselves within the limits of the bankruptcy law. Sears may have resented the fact that debtors had not paid, but the company was not justified in taking the law into its own hands or profiting at the expense of other creditors.

@ e-COMMERCE AND CYBERLAW

How the Internet Keeps Us Busy at Work and Why Employers Are Watching

The debate continues over the issue of privacy of workers as they use their computers and online access at work. Vault.com, which conducted a survey of workers asking how they use the Internet at work, found that employees use their computers at work for the following nonwork-related activities:

<table>
<thead>
<tr>
<th>Activity</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>News reading</td>
<td>72%</td>
</tr>
<tr>
<td>Travel arrangements</td>
<td>45%</td>
</tr>
<tr>
<td>Shopping</td>
<td>40%</td>
</tr>
<tr>
<td>Job searching</td>
<td>37%</td>
</tr>
<tr>
<td>Special interests</td>
<td>37%</td>
</tr>
<tr>
<td>Stock-checking</td>
<td>34%</td>
</tr>
<tr>
<td>Planning social events</td>
<td>28%</td>
</tr>
<tr>
<td>Instant messaging</td>
<td>26%</td>
</tr>
<tr>
<td>Music downloads</td>
<td>13%</td>
</tr>
<tr>
<td>Games</td>
<td>11%</td>
</tr>
<tr>
<td>Chatting</td>
<td>9%</td>
</tr>
<tr>
<td>Pornography</td>
<td>4%*</td>
</tr>
</tbody>
</table>

Employers have software that enables them to see which Web sites employees have visited, when they visited, and how long they stayed there. Some employers issue reports that indicate which employees are spending large amounts of time online. One employer warned an employee about spending too much time shopping online during work hours and then blocked the sites so that the employee could not access them.

While employees are concerned about privacy, employers are concerned about productivity and the fact that downloading music, for example, can result in the employer’s network jamming or copyright liability. Also, employers are concerned that the types of sites being visited, such as pornographic sites, may result in liability for the employer for an atmosphere of harassment.

The same Vault.com survey found that 90 percent of all employees surfed the Net during work hours for things unrelated to their jobs, and 37 percent had used their computers at work to access the Internet to look for another job. About 13 percent said that they spent two or more hours per working day surfing the Net for things unrelated to their jobs. Ten percent said that they received 21 or more personal e-mails per day at work. However, 53 percent said that they limited their nonwork Internet access to 30 minutes per working day.

Some companies police employee use of computers for employers. Websense, Inc., serves this function for 12,000 companies, including 239 of the Fortune 500 companies. The cost is approximately $15 per employee per year.

Do you think employees should be able to use the Internet for personal items while they are at work? Does it perhaps save time and money to allow employees to do errands via the Internet instead of taking longer lunches and breaks? Is it a breach of privacy for employers to monitor employee use?

SUMMARY

Business ethics is the application of values and standards to business conduct and decisions. These values originate in various sources, from positive (codified) law to natural law to stakeholder values. Business ethics is important because trust is a critical component of good business relationships and free enterprise. A business with values will enjoy the additional competitive advantage of a good reputation and, over the long term, better earnings. When businesses make decisions that violate basic ethical standards, social forces are set into motion and the area of abuse is regulated, with resulting additional costs and restrictions for business. Voluntary value choices by businesses position them for a competitive advantage.

The categories of ethical values in business are truthfulness and integrity, promise keeping, loyalty and avoiding conflicts of interest, fairness, doing no harm, and maintaining confidentiality.

Resolution of ethical dilemmas is possible through the use of various models that require a businessperson to examine the impact of a decision before it is made. These models include stakeholder analysis, the Blanchard and Peale test, the front-page-of-the-newspaper test, the Laura Nash model, and the Wall Street Journal model.

QUESTIONS AND CASE PROBLEMS

1. Marty Mankamyer, the president of the United States Olympic Committee (USOC), resigned in early February 2003 following reports in The Denver Post that indicated she had demanded a commission from a fellow real estate broker in the Colorado Springs area, the home of the USOC, who had sold property to Lloyd Ward, the CEO of the USOC. Mr. Ward had purchased a 1.3-acre lot in Colorado Springs for $475,000 and had paid the listing broker, Brigette Ruskin, a commission. Ms. Mankamyer allegedly demanded a portion of the commission from Ms. Ruskin, and Ms. Ruskin did send a check. Ms. Mankamyer had shown Mr. Ward and his wife properties in the area when they were being considered for the job and when he was considering taking the job. However, Mrs. Ward indicated that Ms. Mankamyer did not identify herself as a real estate agent and she assumed that Ms. Mankamyer was showing the properties as a “goodwill gesture.” What conflicts of interest do you see here?

2. Ann Elkin, who works for Brill Co., has been sent out to conduct two customer evaluations, which have gone much more quickly than Ann anticipated. Her supervisor does not expect Ann back until after lunch. It is now 10:30 A.M., and Ann would like to run some personal errands and then go to lunch before returning to work at 1:00 P.M. Should Ann take the time? Would you? Why or why not? Be sure to consider the categories of ethical values and apply one or two models before reaching your conclusion.

3. Fred Sanguine is a New York City produce broker. Ned Santini is a 19-year-old college student who works for Sanguine from 4:00 A.M. until 7:00 A.M. each weekday before he attends classes at Pace University. Fred has instructed Ned on the proper packing of produce as follows: “Look, put the bad and small cherries at the bottom. Do the same with the strawberries and blueberries. Put the best fruit on top and hide the bad stuff at the bottom. This way I get top dollar on all that I sell.” Ned is uncomfortable about the instructions, but, as he explains to his roommate, “It’s not me doing it. I’m just following orders. Besides, I need the job.” Should Ned just follow instructions? Is the manner in which the fruit is packed unethical? Would you do it? Why or why not? Is anyone really harmed by the practice?

4. Alan Gellen is the facilities manager for the city of Milwaukee and makes all final decisions on purchasing items such as chairs and lights as well as other supplies and materials. Alan also makes the final decisions for the award of contracts to food vendors at event sites. Grand Beef Franks has submitted a bid to be one of the city’s vendors. Alan went to school with Grand Beef’s owner, Steve Grand, who phones Alan and explains that Grand Beef owns a condominium in Maui that Alan could use. Steve’s offer to Alan is: “All it would cost you for a vacation is your airfare. The condo is fully stocked with food. Just let me know.” Should Alan take the offer? Would you? Be sure to determine which category of ethical values this situation involves, and apply several models as you resolve the question of whether Alan should accept the invitation.

5. Television network CNBC and other television networks have been working to develop policies for their business correspondents and guests on their business shows because of a practice known as “pump-and-dump.” Pump-and-dump is the practice of a Wall Street professional or network business correspondent

appearing on television to tout a particular stock as being a good buy. Often, unbeknownst to the viewing audience, the guest or correspondent promoting the stock has a large holding in that stock and, after the television show runs and the stock price creeps up, sells his or her interest at a higher price than would have been possible before the show on which the person raved about the stock. What category of ethical issue exists here? If you were a network executive, what would you do to remedy the problem? Could the government regulate such practices? What kind of regulation could it impose?

6. Adam Smith wrote the following in The Theory of Moral Sentiments:

In the practice of the other virtues, our conduct should rather be directed by a certain idea of propriety, by a certain taste for a particular tenor of conduct, than by any regard to a precise maxim or rule; and we should consider the end and foundation of the rule, more than the rule itself.²⁰

Do you think Adam Smith adhered to positive law as his ethical standard? Was he a moral relativist? Does his quote match stakeholder analysis? What would his ethical posture be on violating the law?

7. If you were asked by your new employer to reveal your salary at your previous job, would you include your bonus as part of your salary, or would you choose not to reveal the bonus? Why would you reveal or not reveal the bonus?

8. Marv Albert, the longtime NBC sportscaster famous for his “Yes!” commentary, was charged with violations of several Virginia statutes, including criminal assault, battery, and sodomy, for his alleged conduct with a woman in a hotel room. Initially, Albert went to trial on the case and denied that the charges were true. During the trial, another woman testified that Albert had engaged in similar behavior with her. Following plea negotiations, Albert entered a guilty plea the next day. He was then fired by NBC under a provision in the contract that prohibited employees from making false statements. Albert had assured his superiors at NBC that the charges were baseless. Do you agree with NBC’s decision to fire Albert? Was his personal behavior relevant for his job performance? Do you agree that lying to your employer should result in automatic termination? Albert is back as a network commentator. Does his reinstatement mean that moral issues and private conduct are irrelevant in business decisions?

9. In 1997, the Federal Trade Commission (FTC) issued a cease-and-desist order against Toys “R” Us. The order required Toys “R” Us to stop what the FTC calls its “blacklisting” practices. The FTC ruled that Toys “R” Us had forced large toy manufacturers, such as Mattel and Hasbro, to withhold their products from such discount warehouse stores as Sam’s Club and Costco. Toys “R” Us allegedly threatened not to carry these companies’ products if they were also sold at the discount warehouse chains. Mattel’s Barbie doll is one example of a toy that Toys “R” Us carried that the discount warehouses were not permitted to carry. Costco CEO James Sinegal said, “You could fill Madison Square Garden with the people who don’t want to sell to us.” Are these types of sales agreements ethical? Is it fair for Toys “R” Us to insist on these arrangements? How do you think these arrangements would affect price?

10. The president and athletic director at the University of California at Los Angeles (UCLA) fired the school’s basketball coach because an expense form he had submitted for reimbursement had the names of two students he said had joined him for a recruiting dinner. The students had not been to the dinner. The coach was stunned because he had been at UCLA for eight years and had established a winning program. He said, “And to throw it all away on a meal?” Do you agree with the coach’s assessment? Was it too harsh to fire him for one inaccurate expense form? Did the coach commit an ethical breach?

11. A new trend is emerging in health insurance: premium increases based on claims. It is common practice in the auto insurance industry, for example, for insurers to revisit your premium each year and adjust it based on factors such as your driving record or number of accidents. However, health insurers have generally evaluated their insured’s health only once, at the outset, when issuing a policy. The reevaluation of health and premiums was a practice that ended in the 1950s because the insurers feared regulators would impose limitations on premiums. At least one health insurer, however, has begun to evaluate the health of its insureds annually and to adjust policy premiums accordingly. Even without examination of insureds, some insurers have increased the insureds’ premiums based simply on the nature of their claims for the year and the possibility that more claims will arise. Those who are healthy are in favor of this annual review. Perceiving themselves as the equivalent of good drivers, they want to pay less when they stay healthy. The health discount is, in their minds, the equivalent of the safe driver discount. However, those who are less healthy argue that people buy insurance so it will be there when they need it, and the coverage should apply without regard to claims. Consider the ethical issues in this type of pricing for health insurance.

12. David A. Vise, a Pulitzer Prize winner and a reporter for the Washington Post, wrote a book entitled The Bureau and the Mole. When the book hit the market,
Mr. Vise purchased 20,000 copies via Barnes & Noble.com, taking advantage of both free shipping offered by the publisher and a discounted initial price. Mr. Vise’s book had already hit the New York Times’ bestseller list in the week before the purchases. He used the books he purchased to conduct online sales of autographed copies of the books, and then returned 17,500 books and asked for his money back. However, that return of 17,500 books represented more books than a publisher generally runs for a book. Mr. Vise said that he did not intend to manipulate the market or profit from the transactions. He said his only intent was to “increase awareness of The Bureau and the Mole.” Mr. Vise’s editor offered to pay Barnes & Noble for any expenses it incurred. Was it ethical to do what Mr. Vise did? Was he within his rights to return the books? What are his remedies? Does Barnes & Noble have any rights?

13. Suzy Wetlaufer, editor of the Harvard Business Review, interviewed former General Electric CEO, Jack Welch, for a piece in the business magazine. In December 2001, she asked that the piece be withdrawn because her objectivity might have been compromised. Those at the magazine did another interview and published that interview in the February issue of the magazine. Editorial director of the magazine, Walter Kiechel, who supervised Ms. Wetlaufer, acknowledged as true a report in the Wall Street Journal about an alleged affair between Ms. Wetlaufer and Mr. Welch and that Mr. Welch’s wife had called to protest the article’s objectivity. Mr. Welch refused to confirm or deny an affair with Ms. Wetlaufer, who was divorced. Some staff members asked that Ms. Wetlaufer resign from her $277,000-per-year job, but she refused. Their objections were that she compromised her journalistic integrity. Mr. Kiechel, on the other hand, noted that she did “the right thing in raising her concerns.” About six weeks later, Ms. Wetlaufer did resign from her position as editor, announcing that she would be spending time with her four children. Do you think there was a conflict of interest if there was an affair between Welch and Wetlaufer?

14. Piper High School in Piper, Kansas, a town located about 20 miles west of Kansas City, experienced national attention because of questions about students and their term papers in a class in botany. Christine Pelton, a high school science teacher, had warned students in her sophomore class not to use papers posted on the Internet for their projects. When their projects were turned in, Ms. Pelton noticed that the writing in some of the papers was well above the students’ usual quality and ability. She found that 28 of her 118 students had taken substantial portions of their papers from the Internet. She gave the students a “0” grade on their term paper projects, with the result that many of the students were going to fail the course for that semester. The students’ parents protested, and the school board ordered Ms. Pelton to raise the grades. She resigned in protest. She received a substantial number of job offers from around the country following her resignation. Nearly half of the high school faculty as well as its principal announced their plans to resign at the end of the year. Several of the parents pointed to the fact that there was no explanation in the Piper High School handbook on plagiarism. They also said that the students were unclear about what could be used, when they had to reword, and when quotations marks were necessary. The annual Rutgers University survey on academic cheating has revealed that 15 percent of college papers turned in for grades are completely copied from the Internet. Do you think such copying is unethical? Why do we worry about such conduct? Isn’t this conduct just a function of the Internet? Isn’t it accepted behavior?

15. Pharmaceutical companies, faced with the uphill battle of getting doctors to take a look at their new products, have created complex systems and programs for enticing doctors to come, sit, and absorb information about the new products. Following is a list of the various type of benefits and gifts that drug companies have given doctors over the past few years to try and get them to consider prescribing their new offerings:

- An event called “Why Cook?” in which doctors were given the chance to review drug studies and product information at a restaurant as their meals were being prepared—they could leave as soon as their meals were ready, and they were treated to appetizers and drinks as they waited
- Events at Christmas tree lots where doctors can come and review materials and pick up a free Christmas tree
- Flowers sent to doctors’ offices on Valentine’s Day with materials attached
- Manicures as they study materials on new drugs
- Pedicures as they study materials on new drugs
- Free car washes, and they can study materials while their cars are being washed
- Free books with materials enclosed
- Free CDs with materials attached
- Bottles of wine with materials attached
- Events at Barnes & Noble where doctors can browse and pick out a book for themselves for free as long as they also take some materials on a new drug

Some doctors say that they can enjoy dinner on a drug company as often as five times per week. The American Medical Association (AMA) frowns on the

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21Del Jones, “Editor Linked with Welch Finds Job at Risk,” USA Today, March 5, 2002, 3B.
22Ms. Wetlaufer and Mr. Welch were engaged to be married after Mr. Welch divorced Jane Welch.
“dine-and-dash” format because its rules provide that dinners are acceptable only as long as the doctors sit and learn something from a featured speaker. The AMA also limits gifts to those of a “minimal value” that should be related to their patients, such as notepads and pens with the new drug’s name imprinted on them. The chairman of the AMA Committee on Ethics says the following about gifts, “There are doctors who say, ‘I always do what’s best for my patients, and these gifts and dinners and trips do not influence me.’ They are wrong.”23 In which category of ethical issues do these gifts fall? Do you think doctors act ethically in accepting gifts, meals, and favors? The Food and Drug Administration recently issued rules about such favors and perks. Why?


WEB SITE REFERENCES

Go to http://www.inc.com and type “ethics” in the site search for a look at sample codes of ethics, ethical dilemmas, and ethics programs.

Visit also the Web site for the Markula Ethics Center of Santa Clara University:
http://www.scu.edu/Ethics/
Note: The E must be uppercase.

Visit the Ethics Resource Center and review types of ethics programs and ethics surveys:
http://www.ethics.org

Visit an institute that focuses on ethics in international business:
http://www.globalethics.org

Visit the Josephson Institute, an organization that researches current ethical standards:
http://www.josephsoninstitute.org