

## CHAPTER 3

# ***ETHICS AND CORPORATE SOCIAL RESPONSIBILITY***

### **Learning Objectives**

After reading this chapter, the student should be able to:

- Differentiate between various ethical frameworks and describe how they influence the way managers navigate complex ethical decisions.
- Describe the different types of moral dilemmas that managers face both inside and outside their organizations.
- Explain the ethical, legal, and financial obligations of a business and how these influence a firm's approach to corporate social responsibility.
- Outline the link between corporate social responsibility and the overall performance of a firm.

### **Chapter Outline**

- Introduction
- Ethical Frameworks
  - Utilitarianism
  - Kantianism
  - Virtues and Character
  - Justice

- Moral Dilemmas
  - Common Moral Dilemmas Faced by Organizations
  - The Role of the Individual in Confronting Moral Dilemmas
- Corporate Social Responsibility
  - Economic, Legal, and Ethical Responsibilities
  - Corporate Social Responsiveness
- Is Corporate Social Responsibility Good for Business?
  - CSR as a Competitive Advantage
- Summary

### Self-Reflection: What Are Your Ethical Beliefs?

This self-reflection is designed to assess students’ ethical beliefs. Our ethical beliefs are influenced by life experiences, cultural heritage, values, and a moral compass.

This assessment has 9 questions. For each question, students should respond “True” or “False”.

<i>Self-Reflection Question</i>	<i>Ethical Beliefs</i>
Q1	Believes behaviors are considered moral if they produce the greatest good for the greatest number of people.
Q2	Believes right or wrong actions should be judged solely by the consequences of the actions, not the intent.
Q3	Believes people should maximize the total good of their actions even if this means rules are violated.

Q4	Believes rules are designed to produce good consequences.
Q5	Believes motives are important when judging ethical behavior.
Q6	Believes people should use a standardized process when making ethical decisions.
Q7	Believes when people confront a difficult decision, their values or morals should guide their actions.
Q8	Believes ethical behaviors are the result of societal roles and confronting societal expectations.
Q9	Believes an evaluation of ethical practices should consider differences in the values, opinions, and beliefs of others.
Q10	Believes managers should consider the social aspect of their decisions.

After completing the assessment, students can reflect upon what their ethical beliefs are and how ethical beliefs influence managerial behaviors.

## Comprehensive Lecture Outline

- I. **Introduction. Ethics** is the study of moral standards and their effect on behavior and conduct. **Morality** is defined as the standards people use to judge what is right or wrong, good or evil. Although this may seem like a simple concept, the study of ethics is one of the most complex topics in business. What, on the surface, may seem like a simple choice between right and wrong is not always so simple, especially when there are personal costs that one must pay. As a manager, you will face pressures from your boss, your shareholders, your customers, and your subordinates to satisfy economic, legal, and ethical obligations. Rarely do these interests align. As organizations become more global, they are inevitably confronted with various ethical dilemmas and competing priorities. An increasingly important lens by which organizations are

evaluated both domestically and globally is whether they are responsible corporate citizens.

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**Class Activity:** Use the case below as an opportunity to allow students to apply concepts from the chapter. Suggestion: You could ask them to do this case as individuals or in teams as a class activity. Have the students read the case presented in the text and answer the included questions.

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### **Case In Point: Merck and River Blindness**

A. Why was Merck hesitant about developing a human version of Ivermectin?

Merck was hesitant about developing a human version of Ivermectin because the company faced worsening economic conditions and industry pressures. This included rising healthcare costs, limited Medicare and Medicaid reimbursements, and potential legislation that would make it easier for competitors to copy and market generic drugs.

B. What would be the benefits and cost of developing a human version of Ivermectin?

The benefits of developing a human version of Ivermectin is that the drug may provide a low-cost, safe, and simple cure for river blindness. However, developing the drug would cost Merck approximately \$100 million and many victims of river blindness were too poor to afford the drug. Also, there was not an easy way to distribute the drug to rural areas and there was the possibility that people would misuse the drug. The misuse of the drug could cause negative side effects that may stimulate bad press for Merck.

C. Why did Dr. P. Roy Vagelos and his team decide to develop a human version of Ivermectin?

Dr. P. Roy Vagelos and his team decided to develop a human version of Ivermectin because they came to the conclusion that the human benefits of a drug for river blindness were too significant to ignore. The team believed they were morally obligated to develop the drug despite the costs and slim chance of economic reward.

- D. How do you think Merck's investments in the human version of Ivermectin create value for its stakeholders and corporate goodwill?

Merck's investments in the human version of Ivermectin created value for its stakeholders and corporate goodwill because the firm became known for its ethically and socially responsible behavior. This provided Merck with marketing and reputational advantages.

## II. Ethical Frameworks

- A. **Utilitarianism.** The ethical philosophy claiming that behaviors are considered moral if they produce the greatest good, or utility, for the greatest number of people.
- B. **Kantianism.** An ethical philosophy claiming that motives are the most important aspect in judging what is right or wrong; only good motives build trust. Kant also believed that all humans deserve respect and that actions should be judged based on universal law.
- C. **Virtues and Character.** Virtue ethics claims that morality's primary function is to develop virtuous character. Kohlberg's research outlined three levels of moral development.
1. Preconventional morality usually occurs earlier in life during childhood.
  2. Conventional morality happens as people transition from highly dependent children to more independent adolescents.
  3. Postconventional morality is exhibited by those with a higher awareness of moral values.

- D. **Justice.** Provides the framework for society to judge what is morally right or wrong, fair or unfair, and establishes ways to evaluate or punish those who behave in morally wrong ways. Justice is the notion that moral behaviors must be based on standards of equity, fairness, and impartiality to preserve order in society.
1. Distributive justice deals with the distribution of wealth and among members of a society.
  2. Procedural justice is the notion that rules should be clearly stated, consistently obeyed, and impartially enforced.

### **The Leadership Development Journey**

For this assignment, students are asked to think about how leaders are responsible for creating ethical climates in their organizations. Students are provided with the following list of areas in which leaders can incorporate ethical practices and behaviors.

- Recruiting and selecting employees
- Onboarding and training employees
- Instituting policies and codes
- Rewarding and punishing behavior
- Maintaining managerial-accounting systems
- Supervising performance-management systems
- Managing decision-making processes

Using this list as a starting point, students should consider a time when they observed a leader creating an ethical climate and answer the following questions.

- How did this leader inspire and motivate ethical behavior?
- What were the support systems that reinforced this leader’s ethical standard?
- What did they learn from this leader’s ethical behavior?
- How will they apply the lessons learned to their leadership development journey?

**III. Moral Dilemmas.** Ethical dilemmas are rarely as simple as knowing what is right or wrong. While many people believe that they are ethical in the workplace, most people fall far short of self-perceived morality. The complexities of ethical decision making include ambiguous situations, personal biases, and organizational influences.

A. **Fiduciary Relationships.** Exists when a party—an individual or a business—is entrusted with property, information, or power to make decisions on behalf of another party. The fiduciary is obligated to be candid with his or her beneficiary and disclose all relevant information. Fiduciaries also have a duty of undivided loyalty, which means that they must not only protect and promote their beneficiary’s interests, but also avoid putting their own interests ahead of the beneficiary’s.

B. **Common Moral Dilemmas Faced by Organizations**

As the United States industrialized during the twentieth century, businesses made sweeping progress in their actions regarding the environment, consumers, and employees. This progress was a result of force of law, pressure from advocacy groups, or company choice. As the economy transitions from the manufacturing age to the information age, moral dilemmas now often involve the transmission of information.

1. **Environmental Dilemmas.**

a. **Pollution.** Managers must determine the balance between their ethical obligations to the environment and the costs incurred by their business.

- b. **Resource Depletion.** Companies often have to weigh short-term efficiency and profitability against long-term environmental sustainability. In many cases, companies and managers make choices that favor the short term, which can result in disastrous consequences for future generations.
- c. **Privacy Dilemmas.** A person's right to determine the type and extent of information that is disclosed about him or her.

C. **The Role of the Individual in Confronting Moral Dilemmas**

- 1. **Conflicts of Interest.** Conflicts of interest occur when employees or managers engage in activities on behalf of the firm and they have a personal interest in the outcome of those activities.
- 2. **Insider Trading.** Insider trading involves using proprietary information about a stock for personal gain.
- 3. **Trade Secrets.** Trade secrets are any type of information used in conducting business that is not commonly known by others. It often provides a strategic advantage for a firm over its competitors.
- 4. **Bribery.** Organizations can suffer negative economic consequences such as the diversion of resources to inefficient uses, higher costs of doing business, and loss of investor confidence. At the governmental level, bribery undermines economic development because it decreases efficiency, breeds cynicism, and distorts international competition.
- 5. **Whistle-Blowing.** The release of information, by a member of an organization that has evidence of illegal or immoral conduct, to executives in a company or regulating agencies outside a company. Although whistleblowers are acting ethically, they usually pay a high price for their acts of dissent. They can be blacklisted, fired, threatened, and treated unfairly, and they often endure financial hardship.



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**Teaching Tip:** Suggested readings: “‘Good’ Companies Launch More New Products” by Xueming Luo & Shuili Du *Harvard Business Review*; Apr2012, Vol. 90 Issue 4, p28-28.

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**IV. Corporate Social Responsibility.** Corporate social responsibility (CSR) is a business's obligation to pursue policies, decisions, and actions that align with the objectives and values of society.

**A. Economic, Legal, and Ethical Responsibilities**

1. **Economic:** A firm's duty to make a profit and increase shareholder value.
2. **Legal:** A firm's duty to pursue its economic responsibilities within the limits of the law.
3. **Ethical:** A firm's duty to meet the expectations of society beyond its economic and legal responsibilities.

### **A Different View: Strategic Corporate Philanthropy**

For this chapter's A Different View, we recommend that the professor facilitate a discussion on how corporations may find it difficult to justify philanthropic behaviors. As a result, corporations have become be more strategic about their giving by aligning their corporate social responsibilities with their corporate philanthropy.

After this discussion, students should respond to the following questions.

1. Identify a company that has donated generously to their local economy. What are their motives? What social benefits does their donation provide? What benefits does their donation provide to their own organization?
2. Identify a company that is a leader in corporate philanthropy. What are they doing right? How are their donations benefiting society and themselves? What can other organizations learn from them?

3. How can organizations share best practices and learn from each other? How would that help the community as well as their bottom line?

B. **Corporate Social Responsiveness.** The practice of businesses responding to pressure from society to engage in socially responsible ways. Responsive firms are characterized by three behaviors:

1. They monitor and assess environmental conditions on a constant basis.
2. They seek to identify the needs of their stakeholders.
3. They design plans and policies to respond to changing conditions.

V. **Is Corporate Social Responsibility Good for Business?**

A. **CSR and Financial Performance.** Mixed results for CSR studies:

1. Financial indicators indicate lower performance.
2. CSR is an investment that leads to improved efficiency, innovation, and long-term profitability.
3. Consumers have a favorable attitude toward companies engaging in CSR and also make purchasing decisions based on CSR activity.

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**Teaching Tip:** Suggested reading: "Strategy & Society: The Link Between Competitive Advantage and Corporate Social Responsibility" by Porter, Michael E. and Kramer, Mark R., *Harvard Business Review*; Dec2006, Vol. 84 Issue 12, p78-92.

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B. **CSR and Strategy: Using CSR for a Competitive Advantage.** Strategic CSR Corporate social responsibility activities that are directly related to their business activities so that they can combine social welfare with financial welfare.

1. Supporting Core Business Activities

CSR is strategic when it supports core business activities that contribute to a firm's mission, vision, and strategy. One of the most important areas is the labor force. By attracting a higher-quality workforce, firms can develop a competitive advantage.

2. Creating a Strategic CSR Platform. Corporate social responsibility activities that are directly related to business activities so that they can combine social welfare with financial welfare. Four steps:

- a. Identify the inside-out linkages as well as the outside-in linkages.
- b. Choose what social issues to address.
- c. Create a corporate social agenda that supports both inside-out and outside-in dimensions.
- d. Add a social dimension to their value proposition.

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**Class Activity:** Use the Management Research Question 1 below as an opportunity to allow students to apply concepts from the chapter. Suggestion: The theatrical movie, *The Insider*, has multiple scenes regarding ethics, social responsibility, etc. Website:

<http://www.imdb.com/title/tt0140352/>

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## Discussion Topics

1. Think about your personal values and beliefs. Where did your values come from? What or who shaped your perspectives on business and leadership?
2. Compare and contrast utilitarianism and Kantianism. How are these ethical frameworks similar and different? Which one is more aligned with your personal values? Why?
3. Do businesses have a moral obligation to the development of society? Is the moral obligation the same or different in emerging markets?
4. Review the stages of moral development in Table 3.1. How might each stage influence the way an individual leads?
5. What incentives or situations might cause someone to struggle with conflicts of interests or trade secrets? How can a company ensure that its employees do the right thing?
6. What motivates a student to cheat in class or to plagiarize a paper?
7. Why do whistle-blowers pay a high personal price for their actions?
8. How should a business evaluate its obligations to the environment?
9. Why should a firm pursue corporate social responsibility? What are the right and wrong reasons for pursuing CSR?
10. Consider the economic, legal, and ethical responsibilities of a business. Which one is most important? Least important?

## Assignments

### *Management Research*

1. For this assignment, students should consider a film that portrays business managers and focuses on an ethical dilemma. Have students respond to the following questions about the film.
  - What was the ethical issue in this film?
  - What was management's role in creating the ethical issue?
  - Did stakeholders pressure management to resolve the ethical issue?
  
2. For this assignment, students should research a company that has been included on the Ethisphere Institute World's Most Ethical Companies. Have students answer the following questions about the company.
  - What are its ethical management practices?
  - How do you think organizational culture and leadership action influence these ethical practices?
  - How do you think this company's investment in ethical practices creates value for its stakeholders?
  - Does this company create synergies between its values, ethics behavior, and corporate community?

### *In the Field*

For this assignment, students should select an organization in their community to conduct an ethics and corporate social responsibility audit. Students should use the checklist below to evaluate the organization's ethical management practices and corporate social responsibility practices using the following checklist.

- If the organization has a code of conduct that defines appropriate behavior for its members, review it.
- Identify if the organization has a training program for ethics. If the organization has a training program, what is the curriculum?
- Does this organization have a system of check and balances for managing its financial resources?
- How does the organization incorporate ethics and corporate social responsibility into its strategic planning process?
- Are employees evaluated and rewarded for ethical behavior?
- How does the organization punish inappropriate ethical behavior?
- Does the organization have performance metrics for its corporate social responsibility initiatives?
- Does the organization publicly report its corporate social responsibility initiatives?

After the completion of this assignment, have students compare their ethics and corporate social responsibility audits and discuss how they can help organizations improve their practices.