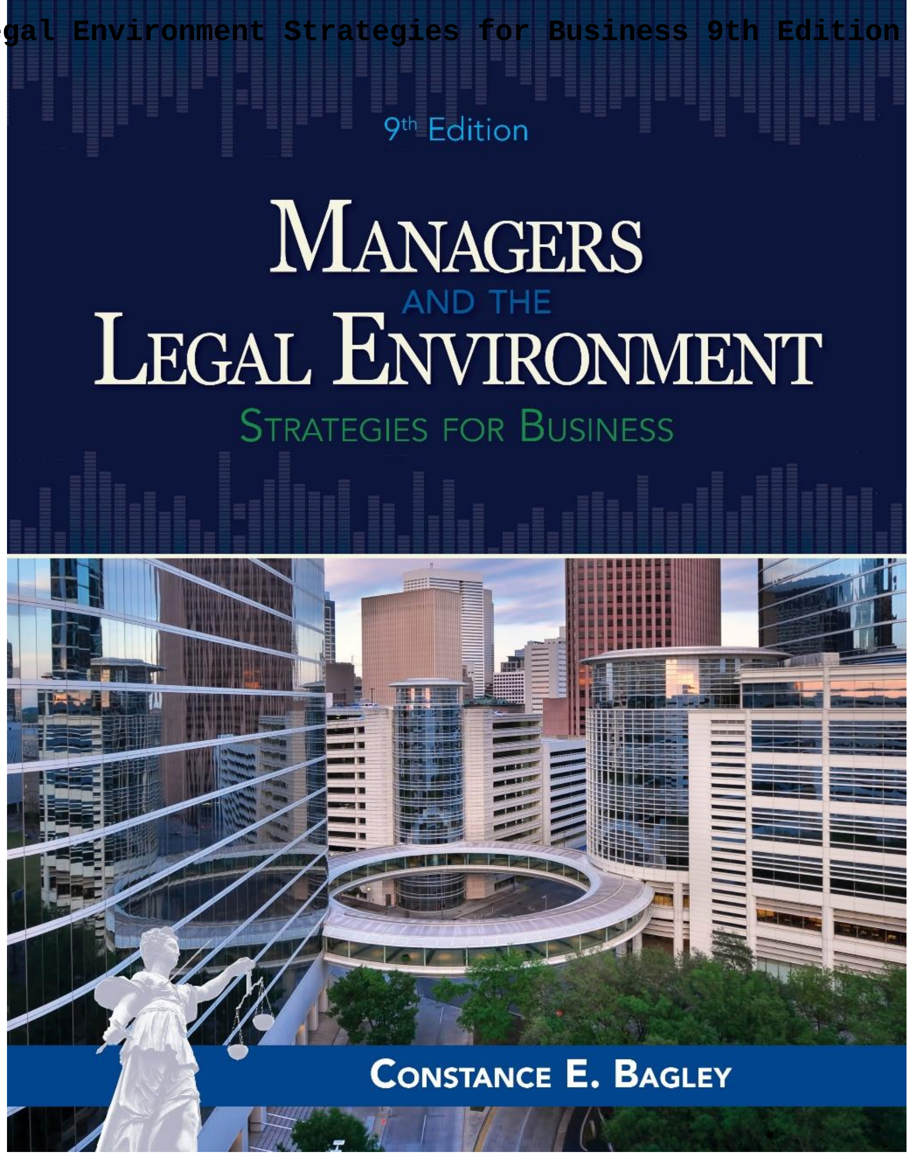

Answers to *A Manager's Dilemma* and
Questions and Case Problems
to Accompany

MANAGERS AND THE LEGAL ENVIRONMENT
STRATEGIES FOR BUSINESS

Ninth Edition

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Chapter One

Law, Value Creation, and Risk Management

A MANAGER'S DILEMMA: PUTTING IT INTO PRACTICE

JPMorgan and Its Hiring Practices in China: Networking or Bribery?

***Issue Presented*: What procedures should a new manager of a company with operations in China put in place to ensure that your company does not violate the Foreign Corrupt Practices Act (FCPA) when making hiring decisions? How will you respond if you learn that a non-U.S. competitor has offered to hire "qualified" sons and daughters of government officials for summer internships?**

Whenever engaging in international business development, managers are expected to exercise their responsibilities according to the laws and practices of the countries where they conduct business. However, a manager should also consider the ethical standards in the home country, where the firm is headquartered and where the board of directors will review his or her performance, as well as what the shareholders would consider ethically acceptable.

The manager must comply with the U.S. Foreign Corrupt Practices Act, which is discussed in Chapter 24. The manager should consult with qualified counsel to ensure that the firm's hiring practices fall within the scope of both U.S. and Chinese law. The FCPA prohibits any payment by a company, its employees, or its agents directly or indirectly to a foreign government official or a foreign political party for the purpose of improperly influencing government decisions to obtain business abroad. The statute is violated even if the bribe is only offered but never paid. Although managers may be tempted to carry out illegal practices by using agents or intermediaries (who may include shipping and customs agents, vendors, and contractors who are under less direct control and supervision by the company making the payment), the FCPA attempts to stem this practice by establishing two sources of intermediary liability: (1) The act's anti-bribery provision makes it unlawful to make a payment to an intermediary knowing that all or part of that payment is going to be made to a foreign official for the purpose of influencing that official to obtain business; and (2) the act's record-keeping provisions require companies to exercise due diligence and implement internal controls to ensure that payments to intermediaries are properly classified and not disguised bribes.

Hiring the children of government officials is common in China, particularly in the banking industry, and that business practice must be carefully weighed against the strictures of the FCPA and American expectations of ethical business conduct. Even though it might be difficult to establish that hiring a particular individual resulted in business with a government official who was related to that individual, U.S. regulators are increasing their investigations in this arena. For example, it would likely be easier to prove a violation of the FCPA where "hard" evidence, such as invoices or receipts, showed that lavish dinners or gifts had been given to government officials and that business contracts with those officials subsequently arose. This situation involves the benefit of human relationships, something that is difficult to measure. As such, all aspects of the firm's hiring practices could potentially be scrutinized by government regulators both in the United States and China, including its recruitment strategies, the prior experience and performance evaluations of the individuals hired, and email correspondence with the government officials. A manager should also review the firm's code of conduct and take full advantage of any ombudsperson available. Although some firms apply different ethical standards depending on the country in which they are doing business, others (such as General Electric) have uniform global standards they apply to all their operations. Finally, while often difficult in practice, the manager should not sacrifice his or her personal integrity.

If a manager learns that a non-U.S. competitor has offered to hire "qualified" sons and daughters of government officials for summer internships, the manager should not sacrifice his or her personal integrity or violate the law to win future business. Although it may be difficult at times to maintain market share or compete successfully, the consequences of not complying with the FCPA are serious. If a manager becomes aware that "qualified" relatives are being hired by other firms, he or she should use such knowledge to make sure that the hiring practices in his or her own company are "squeaky clean," as the U.S. Department of Justice aggressively pursues offenders of the act.

JP Morgan Chase ultimately paid $264 million in fines to settle charges that it won business from clients and corruptly influenced government officials in the Asia-Pacific region by giving jobs and internships to their relatives and friends in violation of the FCPA. Press Release, SEC, JP Morgan Chase Paying $264 Million to Settle FCPA Charges (Nov. 17, 2016), https://www.sec.gov/news/pressrelease/2016-241.html. According to the SEC,

> investment bankers at JPMorgan's subsidiary in Asia created a client referral hiring program that bypassed the firm's normal hiring process and rewarded job candidates referred by client executives and influential government officials with well-paying, career-building JPMorgan employment.

The SEC characterized the hired children as "typically unqualified for the positions on their own merit," and stated that "[t]he misconduct was so blatant that JPMorgan investment bankers created 'Referral Hires vs Revenue' spreadsheets to track the money flow from clients whose referrals were rewarded with jobs. The firm's internal controls were so weak that not a single referral hire request was denied."

QUESTIONS AND CASE PROBLEMS

Question 1.1

Issues Presented: **What public policies are furthered by this law? To what extent are there conflicts among the policies served and how will they affect the way the law in this area is interpreted, applied, and changed?**

The laws and regulations applicable to U.S. business in the early twenty-first century further four primary public objectives: promoting economic growth, protecting workers, promoting consumer welfare, and promoting public welfare. Other major economic powers tend to have laws that further these same objectives, albeit with varying degrees of emphasis on the different objectives and varying ways of furthering them. Indeed, much of the current debate on what constitutes good corporate governance turns on how much weight each country gives to the interests of shareholders, debtholders, employees, customers, and suppliers and to the protection of the environment.

Sometimes those objectives may conflict. For example, intellectual property protection may promote economic growth by giving incentives to innovate but may also create barriers to entry and increase the likelihood of monopoly pricing, to the detriment of consumers.

Question 1.2

Issue Presented: **What effect does this body of law or legal tool have on the competitive environment and the firm's resources?**

Law helps shape the competitive environment and affects each of the five forces that determine the attractiveness of an industry (buyer power, supplier power, the competitive threat posed by current rivals, the availability of substitutes, and the threat of new entrants). Law also affects the allocation, marshaling, value, and distinctiveness of the firm's resources. Under the resource-based view (RBV) of the firm, a firm's resources can be a source of sustained competitive advantage if they are valuable, rare, and imperfectly imitable by competitors and have no strategically equivalent substitutes. Legal astuteness is a valuable dynamic capability. Constance E. Bagley, *The Value of a Legally Astute Top Management Team: A Dynamic Capabilities Approach, in* THE OXFORD HANDBOOK OF DYNAMIC CAPABILITIES (David J. Teece & Sohvi Leih eds., 2016), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2811424. Conversely, failure to integrate law into the development of strategy and of action plans can place a firm at a competitive disadvantage and imperil its economic viability.

Question 1.3

Issue Presented: **Where does this body of law or legal tool fit in the value chain?**

Each activity in the value chain has legal aspects. From a firm's choice of business entity to the warranties it offers and the contracts it negotiates, law pervades the activities of the firm, affecting both its internal organization its external relationships with customers, suppliers, and competitors.

Question 1.4

Issue Presented: **How can managers responsibly help shape this aspect of the legal environment?**

Managers can responsibly help shape this aspect of the legal environment by promoting economic growth, protecting workers, promoting consumer welfare, and promoting public welfare. They can also lobby for stricter laws that raise ethical standards rather than lower them. For example, rather than try to water down the U.S. ban on bribes, a group of firms created Transparency International and fought for international conventions to ban bribery. (This is discussed further in Chapter 2.)

Question 1.5

Issue Presented: **How could the managers in this case have avoided the litigation that ensued?**

At its core, legal astuteness is the ability of the manager to communicate with strategically astute counsel and to work together to solve complex problems. For example, legally astute managers can (1) negotiate contracts as complements to trust building and other relational governance techniques to define and strengthen relationships and reduce transaction costs, (2) protect and enhance the realizable value of the firm's resources, (3) create options through contracts and other legal tools, and (4) convert regulatory constraints into opportunities. Court cases are akin to autopsy reports on transactions gone bad. When reading cases, students should be encouraged to ask how the managers involved could have avoided the dispute or resolved it without resort to litigation.

Question 1.6

Issue Presented: **What are the "moral aspects of choice" implicated by the conduct at issue?**

The systems approach to business and society recognizes that "business decisions consist of continuous, interrelated economic and moral components" and that "moral aspects of choice" are the "final component of strategy." It also builds on stakeholder theory's insight that firms have relationships with many constituent groups, which both affect and are affected by the actions of the firm.

Question 1.7

Issue Presented: **Does this conduct meet societal expectations? If not, what new laws would be likely to result if a substantial number of firms acted this way?**

Legally astute management teams appreciate the importance of meeting society's expectations of appropriate behavior and of treating stakeholders fairly. They accept responsibility for managing the legal dimensions of business and recognize that it is the job of the general manager, not the lawyer, to decide which allocation of resources and rewards makes the most business sense. Complying with the law is just the baseline for determining what course of action to follow. As Ben Heineman, former general counsel of General Electric, put it: "If the first question is, 'What is legal?' than the last should be 'What is right?'" The Foreign Corrupt Practices Act, the Sarbanes-Oxley Act, and the calls for further regulation in the wake of the subprime mortgage crisis are just several examples of how society responds to unethical behavior

Question 1.8

Issue Presented: **Did the manager in this situation exemplify the five components of legal astuteness? If not, what could the manager have done differently?**

The five components of legal astuteness are: (1) a set of value-laden attitudes about the importance of law to the firm's success, (2) a proactive approach to legal issues and regulation, (3) the ability to exercise informed judgment when managing the legal aspects of business, (4) context-specific knowledge of the law and the appropriate use of legal tools, and (5) partnering with strategically astute counsel. Legally astute managers recognize that compliance failures are what Max Bazerman and Michael Watkins call "predictable surprises" and constantly evaluate their products, processes, and business relationships to manage the risk of legal liability.

Chapter Two

Ethics and the Law

A MANAGER'S DILEMMA: PUTTING IT INTO PRACTICE

Deutsche Bank: Looking Into "Mirror Trades"

Issues Presented: **Did the traders at Deutsche Bank violate the law or act unethically when they knowingly engaged in mirror trading? Why do you think the traders acted as they did? Should Deutsche change any of its procedures?**

In January 2017, Deutsche Bank agreed to pay $630 million in fines imposed by financial regulators in the United States and the United Kingdom for engaging in a mirror trading scheme that "laundered $10 billion out of Russia" in trades that "lacked economic purpose" and could have been used to "facilitate money laundering or enable other illicit conduct." Press Release, N.Y State Dep't of Fin. Serv., DFS Fines Deutsche Bank $425 Million for Russian Mirror-Trading Scheme (Jan. 30, 2017), http://www.dfs.ny.gov/about/press/pr1701301.htm. According to New York regulators, the bank failed to maintain an effective and compliant anti-money laundering program; failed to maintain true and accurate books and records; did not respond to a request by a European financial institution about contradictory information about a company involved in the trading scheme; utilized its "Know Your Customer" processes "merely as a checklist with employees mechanically focused" on ensuring paperwork was collected, rather than "shining a critical light on information provided by potential customers"; inaccurately rated country and client risks for money laundering and lacked a global policy "benchmarking its risk appetite"; and understaffed its anti-financial crime and compliance units so much that one compliance staff member said he had to "'beg, borrow, and steal'" to get adequate resources, resulting in existing personnel "scrambling to perform multiple roles." *Id.* As part of its consent order, the bank must engage an independent monitor that will review and report on the elements of the bank's corporate governance that contributed to or facilitated the improper conduct and allowed it to continue, and it must also submit a written action plan to improve and enhance affected compliance programs. In addition to the mirror trading, there was also an "apparent bribe to a Moscow [bank] supervisor" in which $250,000 was "routed" through the bank's Wall Street operation to the banker's wife. Jeffrey Grocott & Gregory White, *How 'Mirror Trades' Moved Billions from Russia: Quick Take Q&A*, BLOOMBERG (June 28, 2017), https://www.bloomberg.com/news/articles/2017-06-28/how-mirror-trades-moved-billions-from-russia-quicktake-q-a.

Economics may have played a part in the scheme, which began in 2011, as "Deutsche traders struggled with a slowdown in business, in the wake of a slump in oil and gas prices as well as the aftermath of the global financial crisis." John O'Donnell, *The 'Mirror' Trades that Caught Deutsche in Russian Web*, REUTERS (Jan. 31, 2017), https://www.reuters.com/article/us-deutsche-mirrortrade-probe-scheme/the-mirror-trades-that-caught-deutsche-in-russian-web-idUSKBN15F23H. Traders apparently did not "forcefully question" suspicious trades because they were earning commissions during a period when trading had "dramatically slowed," with one trader admitting that he was focused on the commissions and continued such trade "despite misgivings." *Id.* The UK regulator also said that compliance staff was "stretched" because of cost-cutting. Mirror trades are "[n]ot necessarily" illegal and do, in certain cases, have legitimate uses. Grocott &White, *supra*. However, when trades do not have an "apparent economic purpose," they should be reviewed with "extra scrutiny." *Id.* Culture may also have played a part—the Russian Central Bank said that Deutsche Bank was not the only international bank that engaged in mirror trades to bypass regulations and get money out of Russia—and one Russian banker said that such trades were "widely considered part of normal business." Evgenia Pismennaya, *Deutsche Bank Wasn't Only 'Mirror' Trader: Russian Central Bank*, BLOOMBERG (June 27, 2017), https://www.bloomberg.com/news/articles/2017-06-27/deutsche-bank-wasn-t-only-mirror-trader-russian-central-bank.

Deutsche Bank shared at least some of the blame. According to the N.Y. regulators, the bank was on "clear notice of serious and widespread compliance issues dating back a decade," and it also knew it was operating in an arena where mirror trading was not uncommon and where an economic downturn existed. *See* Press Release, *supra*. In such an environment, a business entity should take an even stronger role in enforcing compliance with anti-money laundering roles, as well as with its overall ethics policy. In addition to civil charges, and damage to a corporation's reputation, criminal charges may also be filed (in this case, by the U.S. Department of Justice).

When a manager or other employee becomes aware of conduct that looks shady or that appears to be stretching the limits of legality, his or her first step should be to report the conduct to a supervisor. The United States has enacted a number of anti-retaliation laws to protect employees who report employer conduct that violates certain U.S. laws, but even though such laws exist, many employees are understandably hesitant to make such a report, as the loss of a job, or other retaliatory behavior, can be personally and financially devastating. It is worse, however, to become complicit in such activities, under the "everyone's doing it" reasoning and face personal legal liability.

<u>Questions and Case Problems</u>

<u>Question 2.1</u>

Issues Presented: **How should a CEO of a company with a potentially life-saving product defend a significant price increase? Is this ethical or just "good business"? Does making a donation of your product have any bearing on the price increase? When, if ever, should the government become involved in medical product pricing?**

The cost of healthcare in the United States is an often discussed subject, ranging from political opinions about whether the government should fund the cost of healthcare to the confusing realm of insurance policy deductibles, co-pays, and coverage caveats. One subject most consumers agree on, however, is that the cost of certain medical devices and medications is too high, particularly when viewed in tandem with the salaries of the CEOs of pharmaceutical companies.

The increase in a dual-package of EpiPens from $103.50 in 2009 to nearly $609 in 2016 received media attention in part because the salary of Heather Bresch, the CEO of Mylan Pharmaceuticals, increased from almost $2.5 million in 2007 to almost $19 million in 2015. According to Bresch, the price of EpiPens increased about 500% during the last 10 years "because Mylan wanted to make [the product] more accessible," meaning that it had to invest about $1 billion during that time period to reach physicians and educate legislators, as well as "invest[ing] in the supply chain, to make sure that, you know, employers, that employees, that everyone has access to have our medicine." *Mylan CEO on EpiPen Drug Price Controversy: "I Get the Outrage,"* CBS NEWS.COM (Jan. 27, 2017), https://www.cbsnews.com/news/epipen-price-hike-controversy-mylan-ceo-heather-bresch-speaks-out/. As part of its plan to reach the "unmet need," the company concentrated on building public awareness and access, and the product is now in over 70,000 schools across the United States and more than 800,000 EpiPens have been donated. In addition, Bresch claims that 90% of patients paid less than $50 for the product, even though the list price is $600. Although donating products to schools and providing rebates so that most consumers allegedly pay only $50 for the product sounds good on paper, is there any more to Mylan's marketing strategy?

Bloomberg called Mylan's marketing strategy a "textbook case in savvy branding," and also highlighted certain facts unique to the product. Emily Willingham, Contributor, *Why Did Mylan Hike EpiPen Prices 400%? Because They Could*, FORBES (Aug. 21, 2016), https://www.forbes.com/sites/emilywillingham/2016/08/21/why-did-mylan-hike-epipen-prices-400-because-they-could/#72d3203b280c. "[O]ne important detail," highlighted by a parent, was that when a child has a life-threatening allergy, "you are supposed to have 2 EpiPens at all times" so that in case more than 15 minutes pass between the time the first dose is given and the victim's arrival in an emergency room, a second dose can be given. Willingham, *supra*.. As such, the "dual-package" does not mean a parent can use one pen for home use and give the second pen to the school nurse. Instead, each child really needs two dual packs—one dual pack for school and one dual pack for home. In addition, the pens have a one year life, meaning that often another few hundred dollars has to be spent each year (depending on, for example, a consumer's deductible) for a new package of EpiPens, assuming the pens haven't already been replaced because of an allergic reaction. (As noted in the question, the drug incorporated into the EpiPen costs only a few dollars; it is the delivery mechanism that increases the price.) And, if a parent has more than one child with allergies, the number of packages needed multiples. Mylan used this as an "opportunity to cease selling single pens and begin selling only two-packs." Willingham, *supra*. Whether this is ethical is a question that would no doubt have a different answer depending on whether company management or a parent of an allergic child was asked. Regardless, as a result of the product's unique requirements for use, there is a seemingly endless market for the product, making it easier to reach the "three goals of any pharmaceutical company": (1) finding the target (here, the parents of children with allergies); (2) starting those found on the product; and (3) keeping those consumers. Willingham, *supra*.. Is Mylan on track to meet these goals?

It does appear that Mylan has found its target parents, probably because of a variety of factors including its investment in public awareness and donation of products. Other factors have worked in its favor, too, however, including that rival systems have not been accepted by the public as readily. Certain other products, which contain the same medication, are allegedly more difficult to administer and can result in "critical errors" if users aren't properly trained. Willingham, *supra*. For example, EpiPen requires users to remove one single cap, while another product requires the removal of two caps. Willingham, *supra*. The drug can also be administered via a syringe, but the downside of that method is that the dose might not be as well-calibrated and there is the risk of "injection into a vein, instead of a muscle, which can be fatal." Willingham, *supra*.

With regard to whether Mylan has met its goal to "start" parents using its product, it appears that, without regard to cost, EpiPen is the product of choice. Because of the drug's high cost, Mylan offers certain price concessions. For example, uninsured patients can apply to receive the pens for free, and under another program the product's cost is reduced by $100, meaning that what the patients ultimately pay will be based in part on his or her medical plan deductible. These programs sound great but according to a 2017 lawsuit, Mylan's pricing is not all above board.

In April 2017, a class-action suit was filed against Mylan by a competitor alleging that the company engaged in an illegal scheme to "dramatically" increase the list price of the product over the past 10 years which included Mylan paying pharmacy benefit managers (PBMs), such as CVS Caremark, which handle prescription drug benefit programs for insurers. Dan Mangan, *Mylan Hit with Racketeering Suit Over Big Price Hikes of EpiPen*, CNBC.COM (Apr. 3, 2017), https://www.cnbc. com/ 2017/ 04/03/mylan-hit-with-racketeering-suit-over-big-price-hikes-of-epipen.html. The suit notes that while other companies were trying to market competing products, they were not successful because they didn't pay the same level of rebates that Mylan paid to the PBMs, in essence causing the list price to become a "'completely phony price' that bears little resemblance to the relatively minor cost of producing EpiPen." Mangan, *supra*. The lawsuit asserts that Mylan offered commercial insurance companies, PBMs, and state-based Medicaid agencies deep discounts "conditioned exclusively on [Sanofi-Aventis'] Auvi-Q® not being an [epinephrine auto-injector] drug device that those payors would reimburse for use by U.S. consumers." Complaint, Sanofi-Aventis U.S. LLC v. Mylan Inc., No. 3:17-cv-02763-FLW (D.N.J. Apr. 24, 2017). In addition to alleging violations of consumer protection laws, the suit also alleges the company violated the Racketeer Influenced and Corrupt Organizations (RICO) Act. As such, whether Mylan can meet its third goal of keeping the parents as its customers may be negatively impacted.

Whether Mylan's marketing strategy will pay off may not be known for a while, and the press generated from the recent lawsuit may not help its sales. But, with few viable alternatives out there for another product, it may keep its near monopoly. One product may, however, offer some competition. Auvi-Q® introduced a "convoluted" pricing strategy for its epinephrine auto-injector in January 2017 that would charge patients nothing for the product if they have commercial insurance, regardless of whether the insurance company pays for the product, and it would give the product to families that earned less than $100,000. Matthew Herper, *In Rube Goldberg Price Scheme, EpiPen Competitor Auvi-Q to be Free for Patients, $4,500 for their Insurers*, FORBES (Jan. 19, 2017), https://www.forbes.com/sites/matthewherper/2017/01/19/epipen-competitor-auvi-q-to-be-free-for-most-patients-but-cost-4500-for-insurers-in-rube-goldberg-scheme/#632d20513fe6. And, those who do not qualify to get the product for free but who pay cash will be charged $360. The list price for the product, and the "starting point for insurance companies," however, will be $4,500. Herper, *supra*. The pricing scheme means that Auvi-Q would be the least expensive option for patients with insurance, and cost less than the CVS "no-frills generic injector" it will sell for $100 in collaboration with a drug company. Herper, *supra*. Auvi-Q is about the size of a credit card and gives "verbal directions" on its use, which may be something that would help a "panicked parent or bystander" when a person experiences an allergic reaction. The product was launched with Sanofi-Aventis in 2013, but was withdrawn because of a manufacturing issue, which its manufacturer claims to have fixed.

Should the government get involved in drug and medical device pricing? In countries like England with a single payor system, the government by necessity gets involved because it decides which drugs and medical devices will be paid for. In the United States, the government performs a similar role when handling Medicare and Medicaid claims. Otherwise, the individual insurance companies establish their own formularies and lists of covered devices. Savvy consumers can use free programs like Good Rx to buy drugs at deep discounts from list price. If drug and medical device companies fail to exercise at least some pricing self-restraint, the government and public opinion can push for the development of alternatives and embarrass the company's executives in Congressional hearings and in the press.

Question 2.2

Issue Presented: **Is it unethical for a small company to change its operating policies when a natural disaster strikes to take advantage of the increased business?**

Weather-related natural disasters seem to be increasing in number and severity. In 2017, Hurricane Harvey damaged parts of Texas and Hurricane Irma destroyed parts of Florida and certain Caribbean islands. Hurricane Maria devastated Puerto Rico that same year, leaving many of its residents without clean water and power for months.

Many companies do reap a financial benefit from the increased business a natural disaster causes, particularly small local construction and clean-up firms. The point at which ethical behavior becomes unethical is, however, sometimes hard to determine. Door-to-door solicitation and discounts for customer referrals are common business practices and generally are not unscrupulous. Sales tactics that leave traumatized disaster victims with little time to make a rational decision can be unethical, especially when customers are left with the impression that if they do not accept the offered services, there will not be another opportunity to do so within a reasonable amount of time.

On the other hand, local construction and clean-up companies often operate in a "feast or famine" environment and need to take advantage of business opportunities to survive, regardless of their source. Accepting jobs on a cash-only basis may seem harsh, but the company may not have a line of credit on which to draw, and banking facilities may be off-line. Arriving with supplies left over from a previous job might seem coercive to a homeowner, but it could be the most practical way for the construction company to use all available resources. On-the-spot hiring decisions sound harsh in theory, but small business operators realize that if they walk away from a potential customer, the customer is unlikely, or may be unable, to later commit. Asking for the entire amount of payment before a job is completed can appear overly harsh, even in a disaster situation, but it may not be economically feasible for a contractor to wait for insurance payments. Thus, it may be preferable to just require a substantial up-front payment.

Raising prices during a disaster is not always unethical—sometimes higher prices provide an incentive for others to send resources quickly to disaster-stricken areas, and higher prices can function as an incentive to overuse scarce resources. Regardless, charging twice the normal rate for a particular job when a disaster strikes does seem unethical. Contractors realize that victims may not be thinking rationally and will agree to any price just so the work gets done, and some contractors may capitalize on that. However, contractors may themselves be subject to higher prices by suppliers and must pass that cost on to their customers.

There is no universally agreed upon formula to determine when behavior is ethical. A manager using John Rawls' "veil of ignorance" would ask what they would want the rule to be if they did not know whether they would be the best or worst off. The managers of all businesses, large and small, should review their firm's practices, even during times of disaster, to ensure they are not being unscrupulous. While it might result in the loss of some immediate revenue, customers who are treated fairly may very well use those contractors again. In addition, it builds good will when a vendor pitches in to help the communities in which it does business.

Certain economists take a seemingly "inhumane" view and argue that price-gouging during a disaster actually helps disaster victims. These economists explain that setting price caps on needed supplies (so-called anti-gouging laws enacted in 34 states) eliminate the incentive for people to conserve essential supplies and "discourage extraordinary supply efforts" that would move much-needed goods to affected areas, including dangerous areas. Andrew Ross Sorkin, *Price Gouging Can Aid Victims? Why Some Economists Say Yes*, N.Y. TIMES, Sept. 12, 2017, at B1. Matt Zwolinski, the director of the Center for Ethics, Economics, and Public Policy at the University of San Diego, explained that if a hotel doubles its room price during a disaster, a family that might have rented two rooms (one for the parents and one for their children) might now rent only one room, while a family whose house was damaged but is still habitable might now choose to "tough it out" and not to rent the high-priced room. As such, the available supply is now increased because of the "consumers' economizing behavior"—there are more rooms available now to the people who need them most. Sorkin, *supra*. Another economist points out that if prices are not raised during a disaster, "attentive customers may buy up the whole stock, resell it during the emergency, and price gouge themselves," or store employees might "funnel the scarce goods" to relatives and friends. Sorkin, *supra*. These economists acknowledge that these views might not appear rational when "it comes to trying to protect the poorest" who cannot afford basic necessities.

[*See also* Richard Mize, *Natural Disasters Attract Scammers*, DAILY OKLAHOMAN, May 25, 2013, at 5E; *see also* Chris MacDonald, *Post-Hurricane-Irene Business Ethics Roundup*, BUS. ETHICS BLOG, (Aug. 29, 2011), http://www.businessethicsblog.com/2011/08/29/post-hurricane-irene-business-ehtics-roundup.]

Question 2.3

***Issues Presented*: How should a female employee respond to her male boss's insinuation that he is inviting her to a client meeting for her sex appeal rather than her intelligence and knowledge? Does this constitute illegal sex discrimination? How should the head of human resources respond?**

Bart Wayne, Carmella Bancroft's boss, is clearly acting unethically by telling Carmella that he wants her to attend a client meeting for her sex appeal rather than her intelligence and knowledge of advertising. His behavior, while disrespectful, probably is not sufficiently severe or pervasive to constitute actionable hostile environment sexual discrimination if it occurs only once. See *Faragher v. City of Boca Raton*, 524 U.S. 775 (1998), and the discussion of other hostile environment cases in Chapter 13. If, however, Wayne persists in treating Carmella as "eye candy," then that may be illegal sexual stereotyping under *Price Waterhouse v. Hopkins*, 490 U.S. 228 (1989), *superseded in part by statute*, Civil Rights Act of 1991, Pub. L. No. 102-166, § 107, 105 Stat. 1071 (1991). In that case, Ann Hopkins was denied partnership in Price Waterhouse and was told that she needed to dress more femininely, have her hair styled, and wear more jewelry. The U.S. Supreme Court ruled that sexual stereotyping violated Title VII.

This situation puts Carmella Bancroft in the unfortunate position of having to decide how to react to her boss's behavior. If her boss knew how badly she wanted to work with clients, maybe he was giving her the opportunity she seemed to want at any cost. There is no doubt that this would be a good, first opportunity for her to interact with a client. She might be inclined to go to the meeting and use the opportunity to advance her career and learn from her bosses. However, Carmella cannot help but feel uncomfortable about being treated as "eye candy" for a client. Nonetheless, she risks jeopardizing her position at the company or losing her boss's favor if she complains.

Carmella must, however, consider the long-term ramifications of condoning such unethical behavior. If she knows her boss will behave like that to her, then he most certainly will act the same way toward other female employees. If she can prevent other female employees from experiencing such offensive behavior, she should probably report his behavior to HR. Furthermore, there is a slippery slope argument here: if Carmella shows her boss that she is willing to accept this small, disrespectful situation is she inadvertently giving him the okay to make further improper suggestions? He is not asking for sexual favors in return for a promotion this time, but if he gets away with this behavior, will he be more likely to use female employees in even more degrading ways in the future?

Carmella has worked too hard to get her New York University MBA degree and her position at Scot Wayne More to be degraded and used for her looks. If Carmella does not stand up for herself this time, it is likely that her boss will never respect her for her intelligence and knowledge about advertising.

If Carmella feels comfortable talking to her boss about this matter, she could go to him directly and tell him how she feels. She can tell him that she is not comfortable going to a business meeting if her good looks are the only attribute she brings to the table. She can offer to do whatever preparation might be required so she can be a valuable part of the meeting. She can ask her boss to treat her with more respect in the future and let him know that she will report any similar suggestions to HR. Unfortunately, there is a risk that she could lose her boss's favor if she complains. To help protect against this, she might seek out the manager who interviewed her for the position and ask him or her how to handle it. This may give her "air cover" in the event her boss starts complaining about the quality of her work.

Alternatively, Carmella could report the incident to HR or to an anonymous hot-line if she fears retaliation. HR can advise her on the best course of action, encourage her to report future problems, and talk to her boss in her place. If Carmella's boss makes any more comments like this one, she will have established a pattern of behavior on the record by reporting this incident. HR should certainly speak with her boss and remind him that this behavior is inappropriate and that it is illegal to retaliate against Carmella for complaining. (This is discussed further in Chapter 13.) If it has not already been done, HR should rewrite the company's compliance manual to prohibit these types of remarks about an employee's clothing or looks. If this is already part of company policy, then Wayne's conduct is all the more reprehensible. However, reporting misconduct may not always resolve the situation in a male-dominated business or where a "bro-culture" is tolerated. As noted in the "Inside Story" in Chapter 13, even though a number of female engineers at Uber reported a male manager to HR for sexual harassment, initially nothing was done about it. Ultimately, however, the board of directors ousted the CEO and founder for fostering such a hostile environment for women. Similarly, the #MeToo movement has led to the termination or resignation of members of Congress, TV and movie stars, and business executives accused of sexual misconduct so there is definitely strength in numbers.

This hypothetical is adapted from an example provided in JOSEPH L. BADARACCO, DEFINING MOMENTS: WHEN MANAGERS MUST CHOOSE BETWEEN RIGHT AND RIGHt (1997), that involved race, rather than gender. A young African American investment banker named Lewis was invited to a client meeting simply because of his skin color, and felt awkward about the situation. Lewis was so conflicted that he made a list of pros and cons about whether or not to attend the meeting. For example "opportunity" was a major pro, but "phony" was on the list of cons. An excerpt from his thinking on the matter: "Now his firm was singling him out solely for his skin color, not for his talent. Lewis believed companies and clients should base decisions on performance, competence, and character, not on games of mix and match based on race, gender, and religion. Was including him as a token black really all that different from excluding him because he was black?" *Id*. at 12-13. Professor Badaracco further points out that this is not simply a case of deciding the right thing to do: "The challenge is deciding *which right thing to do.* Lewis has to choose between right and right, on a complex issue of personal integrity. His question was not *whether* to be ethical, it was *how* to be ethical." *Id*. at 13-14. Lewis resolved his dilemma by asking to be part of the presentation to the clients, and therefore enabling himself to feel that he was at the meeting for a reason related to his talent and not just his skin color.

<u>Question 2.4</u>

***Issue Presented:* Is it ever ethical for an employee of a company to accept gifts from an individual or firm that does business or wishes to do business with that company? If so, under what circumstances?**

Rodrigo Juarez should decline the tickets to the Super Bowl offered to him by the makers of Brand One. Juarez is ethically obliged to decline any gift if his business judgment might be affected by such a gift, or if there would even be the appearance that his judgment might be affected. Even small gestures, such as dinner, should be accepted only if there are no strings attached. Given that Juarez is an ardent football fan, it is clear that he would greatly value tickets to the Super Bowl. In addition, there is a strong likelihood that his favorite team, the Steelers, will be there. Given the fact that Juarez must decide whether to cut Brand One's baseball gloves or one of Brand One's competitors from his retail chain's line of children's sports gear, accepting such a valued gift might in fact cloud his judgment. It would most definitely create a suspicion of unfairness. This is particularly true given that the brands are equally profitable and there is no easy way to decide which brand to cut. Even if Juarez were to accept the tickets and then decide to cut Brand One simply so that no one could accuse him of favoritism, this would be unethical. Juarez must make the decision based purely on what is best for his company. As a responsible manager, Juarez's first instinct should be to decline the tickets as politely as possible.

There is sometimes a fine line between business gifts and bribes. A bribe implies a clear-cut intention to win someone's favor. To decide whether the tickets are an out-and-out bribe, we would have to know more about the specific motivations of and information possessed by Brand One. If Brand One often showers significant gifts upon individuals who can make decisions favorable to the company, then it may be fair to say that Brand One in fact uses gifts to get favors. Such a policy would constitute a form of bribery.

It should not make any difference whether the person who offered the tickets to Juarez is a family member or a close friend. Juarez is ethically obligated to decline the tickets, given his position of power with respect to Brand One. In fact, if the representative of Brand One is a relative or friend, Juarez may have an even greater obligation to decline the tickets. Friendship and family ties should be kept separate from business relations and business decisions. Juarez's company has an ethical obligation to treat its suppliers fairly, and require them to compete on genuine competitive issues, not on having personal connections with the company's buyer, or showering the buyer with gifts.

Question 2.5

Issue Presented: **Is it ethical for an employee of a company to accept a gift from a firm whose brand he plans to cut from his company's line of products?**

Under no circumstances should Juarez accept the tickets to the Super Bowl. Even if Brand One is clearly the line that he should cut, it is simply bad business and bad ethics to accept highly valued gifts from a business partner. The more Juarez values the tickets, the stronger the obligation to decline them. Juarez should not pay face value for the tickets. Why risk any perception of favoritism or even just the general perception that the company's buyer is offered valued gifts by his suppliers? Note that Juarez has an easy solution in this particular case—there is always an active, legal Super Bowl tickets market for those willing to pay the going price. Juarez will most likely have to pay far more than face value, however.

Juarez's actions should be the same even if he were sure no one would find out about the gift. Just because an action is not publicly known does not mean it is ethical.

Question 2.6

Issue Presented: **What factors should a manager take into account when deciding whether or not to require a confidentiality agreement as a condition to settling a case?**

Requiring confidentiality agreements as a condition of settlement is a common practice. Confidentiality agreements can enable a company to stave off frivolous "me-too" claims. A manager has a business obligation to settle claims as quickly and reasonably as possible, and confidentiality agreements often seem like a promising way of doing so. Because future plaintiffs will not know the economic particulars associated with a settlement, they may settle for less than the original claimant.

Confidentiality agreements are troublesome, however, when they make it less likely that consumers will learn about a product's defects. General Motors covered up potentially deadly defective ignition switches in its cars for more than a decade by settling cases with confidentiality provisions. A company could gravely jeopardize its public image by covering up damages paid for defective or harmful products. As Chief Judge Joseph F. Anderson Jr. of the U.S. District Court for the District of South Carolina wrote: "Some of the early Firestone tire cases were settled with court-ordered secrecy agreements that kept the Firestone tire problem from coming to light until many years later. Arguably, some lives were lost because judges signed secrecy agreements regarding Firestone tire problems." Judge Anderson refused to approve Firestone's request for a confidential settlement agreement in light of the wider ramifications for society:

"Here is a rare opportunity for our court to do the right thing and take the lead nationally in a time when the Arthur Andersen/Enron/Catholic priest controversies are undermining public confidence in our institutions and causing a growing suspicion of things that are kept secret by public bodies." Adam Liptak, *Judges Seek to Ban Secret Settlements in South Carolina*, N.Y. TIMES, Sept. 2, 2002, at A1. Similarly, companies and other institutions can provide a cover for serial harassers by settling claims with gag orders preventing the victims from telling others about others' misconduct.

Defective products were responsible for deaths and injuries to more than 65,000 babies and small children in 1999, both before and after products had been recalled. In response to injuries, companies often negotiated press releases that made their product sound less dangerous than it really was and thereby avoided extensive press coverage. While the Consumer Product Safety Commission, the federal agency in charge of ensuring the safety of consumer products, strives to get the word out about such dangers, it often does not have the funding or will to force companies to respond appropriately.

Legal norms have changed to require more responsible corporate behavior. After their child was killed by a crib that collapsed, two parents persuaded the Illinois government to enact the Children's Product Safety Act in 1999, which made it illegal to sell a children's product after it has been recalled. Marla Felcher, *Children's Products and Risk*, ATLANTIC MONTHLY, Nov. 2000, at 36–42. The amendments to the Consumer Product Safety Act enacted in 2008 also limit the sale of recalled products.

If prohibiting secret agreements saves lives and prevents further harmful effects, then lawmakers may enact legislation barring secret settlements. On the other hand, confidentiality agreements tend to make companies feel more comfortable releasing sensitive information that otherwise would not come to light. For example, Harvard Law School Professor Arthur Miller responded to Chief Judge Anderson by stating that "the ban on secret settlements would discourage people from filing suits and settling them, and threaten personal privacy and trade secrets." Liptak, *supra*. Responsible managerial restraint, rather than one-size-fits-all regulation, may be the best course of action.

Question 2.7

Issue Presented: **Is it ethical for a consultant to gather information from a company without revealing her association with its direct competitor?**

Ginny Thomas clearly cannot lie about her employer when gathering data; to do so would be fraud. She also should not solicit trade secrets or encourage others to violate any nondisclosure agreements; otherwise, she might violate the Uniform Trade Secrets Act or the Defend Trade Secrets Act of 2016 or be liable for intentional interference with a contract.

Talking with low-level employees would be legal if done in accordance with these strictures. Its ethical character is a closer call. On the one hand, competitors should train their employees not to disclose sensitive data. On the other, taking advantage of low-level employees' ignorance seems questionable. Ideally, she would figure out a way to get permission from the higher level managers, perhaps by offering to share some of the results of the study. In any event, if she personally views the calls as unethical, she should not make them. Instead, she should talk with other consultants and managers in the firm and try to persuade them that she is right or let them persuade her that they are. She might also promote an industry code of conduct that sets high ethical standards, as Chartered Financial Analysts have done.

Question 2.8

Issue Presented: **May an employee accept an expensive prize as a result of participation in a company-sponsored event?**

Although Wendi Wu was clearly meant to be the recipient of the prize under the terms of the contest, she has an ethical obligation to inform her supervisor about the prize and offer it to her employer. The gift is extremely valuable, and she went to the event as a company representative, not as an individual. The company may or may not allow her to keep the home-theatre system. Wu should also consider how her supervisor and others would react to hearing about the home-theatre system gift if she does not tell them herself. Wu should avoid the appearance of impropriety. In grey matters like this one, it is always best to err on the side of caution and act as ethically as possible. The home-theatre system really belongs to the company, since the company sent Wu and could have chosen to send someone else just as easily. If Wu were a manager receiving the home-theatre system (or a similar benefit) as a result of her affiliation with the company, she would have a fiduciary duty, and not just an ethical obligation, to inform the company.

The company should provide in the code of conduct or in the employment contract that gifts or prizes over a certain value received as a result of company affiliation must be reported to the appropriate authorities and offered to the company. This type of policy would have the additional value of discouraging employees from accepting gifts or bribes in general.

If Wu's manager finds out about the prize from a source other than Wu, she should confront Wu. She should explain to Wu that because she received the gift as a result of a company-sponsored event, she