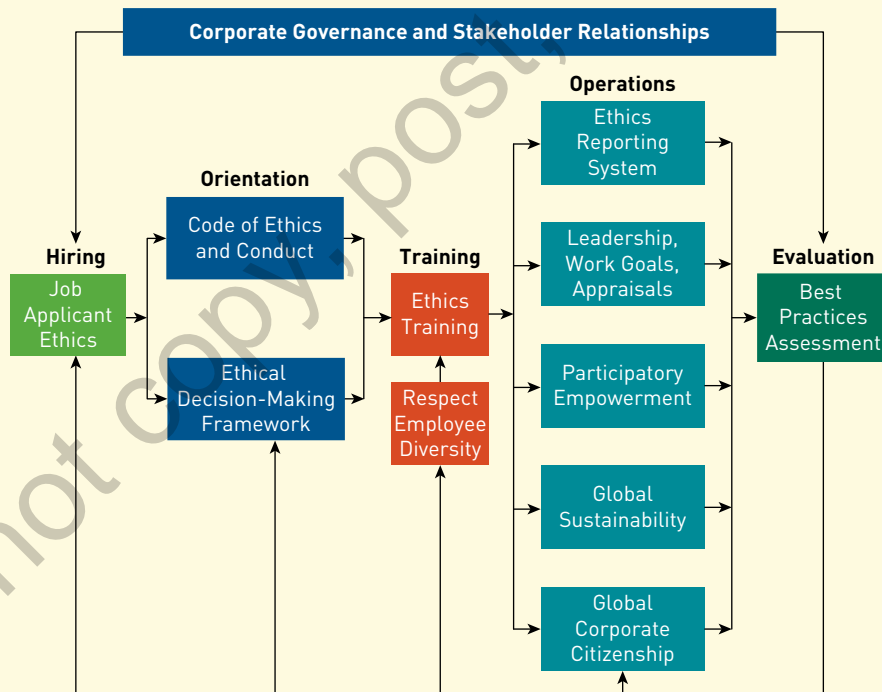


AN INTRODUCTION TO BUSINESS ETHICS

Chapter 1:	Unethical Behaviors in Organizations and Human Nature	3
Chapter 2:	The Evolution of Business Ethics	37
Chapter 3:	Corporate Governance and Stakeholder Relationships	67



Do not copy, post, or distribute



©iStockphoto.com/Michael Blankennagel

1

UNETHICAL BEHAVIORS IN ORGANIZATIONS AND HUMAN NATURE

LEARNING OBJECTIVES

After reading this chapter, you should be able to

- 1.1 Identify common types of unethical behaviors in the workplace.
- 1.2 Describe how unethical behaviors can be very costly to organizations.
- 1.3 Explain the competitive advantages of creating and maintaining an ethical organization.
- 1.4 Describe different theories of human nature as related to ethics at an individual's time of birth.
- 1.5 Explain the stages of moral development.
- 1.6 Discuss why good people occasionally behave unethically and why morality should be practiced.

WHAT WOULD YOU DO? BILLING FOR SERVICES RENDERED

After graduation, you enter a 6-month medical office manager training program associated with a prestigious hospital. The training program consists of 3 weeks in each of various office operations. You greatly enjoyed 3 weeks performing customer service and learning about accounting functions. Your latest 3-week assignment is in the billing department.

Medical bill coding is fascinating and complex. Coders are health care professionals responsible for processing patient data, such as treatment records and related insurance information. Coders translate billable information into medical codes sent to insurance companies for proper reimbursement.

A patient arrives early in the day looking absolutely miserable. Unfortunately, the patient requires treatment not covered by his insurance company. While walking past the examining room you overhear the patient say, "I can't afford paying for the medicine out of pocket." The caring doctor tells the patient not to worry, she can work around that problem. "Thanks doc," the patient says, "you're a lifesaver."

Back in the bill coding department you receive the patient's documents to code. You know the patient was not treated for the illness that appears on the document and point this out to your trainer. "This happens on rare occasions," he tells you. "It's a similar illness, and the insurance companies will never know. They make a fortune from us anyway. On a few occasions they somehow find out, and we just say it was a simple mistake. The doctor has an office account that covers the amount not reimbursed to patients. Everyone does it. Just enter the code for the illness reported by the doctor."

Critical Thinking Questions

1. What *could* you do?
2. What *would* you do?
 - a. Enter the code for the illness reported by the doctor
 - b. Refuse to enter the code for the illness reported by the doctor
 - c. Something else (if so, what?)
3. Why is this the right option to choose?
4. What are the ethics underlying your decision?

ETHICAL ISSUES AT WORK

“*Business ethics*, isn’t that an oxymoron?” The answer to this often-repeated question is no, ethics permeate business activities. Businesses operating based on good ethical principles abound and attract good employees and customers. Businesses lacking good ethics are often held accountable through litigation, lost customers, bad reputations, and high employee turnover.

In general, businesses significantly improve the quality of life by providing goods and services that fulfill consumer needs. Service to others, one of the most admirable ethical principles, is at the heart of business operations.

A **well-managed organization** is a *community of people on a common mission to be effective, efficient, and ethical*. An organization is a community, not just a bunch of individuals, and a community of people who are both rational and emotional, not robots. Your mission as a manager is to develop a sense of a common mission among this community of people to accomplish goals (effective) without wasting resources (efficient), in a manner that respects each person’s dignity and integrity (ethical). The financial well-being of organizations depends on employees appropriately serving the needs of customers, owners, and other employees. If employees are not ethical, then the effectiveness and efficiency accomplishments will be short-lived.

Look around. A business built the house you live in, the alarm clock that wakes you up, the bed you sleep in, the clothes you wear, the cell phone you use, the periodicals you read, the computer you work on, the chair you sit in, the food you eat, the music you listen to, and the car you drive to school or work. Generally, consumers want these products to be trustworthy, otherwise they feel disrespected.

Providing goods and services is just one ethical aspect of business operations. Managing a business is complex because it requires integrating a broad cooperative network of human interactions. Assume you have an idea for a new business. You will need skilled and trustworthy people to help with product development, financing, marketing, accounting, management, and sales. You will be interacting with suppliers as well as customers. Some of the people in your network, and those wanting to become part of your network, may have high ethical standards; some may not.

Well-managed organization Community of people on a common mission to be effective, efficient, and ethical.

An organization's ethical environment must be managed. Because of imperfections in human nature and control systems, all organizations are ethically challenged, some more so than others. The judicial system overflows with lawsuits for alleged wrongdoings filed against organizations by employees, customers, suppliers, and other organizations. Day after day, week after week, and year after year media outlets highlight the latest unethical business activities. The chair you purchased as high quality may have been made by child laborers under harsh working conditions; the website you just clicked on may now be collecting data about your private life. Ethical issues seem endless and influence the public's negative perspectives about business, despite the numerous positive personal interactions individuals have with businesses.

Federal, state, and local governments create new rules and regulations to ensure business stakeholders are treated appropriately. A **stakeholder** is any person or organization that is affected by, or could affect, an organization's goal accomplishment. Regulators are tasked to ensure employees are fairly treated, customers and suppliers are dealt with honestly, and the natural environment is protected.

Ethical behavior at work is a personal choice influenced by an individual's past behaviors and current workplace environment. Some owners and managers choose to surpass the minimum requirements of existing rules and regulations, some choose to meet existing rules and regulations, and others continually exploit loopholes in existing rules and regulations. Stakeholders reward ethical organizations that go beyond compliance with their loyalty and avoid doing business with organizations that violate good business practices.

This chapter discusses why appropriately managing ethics is essential for every organization. The chapter explores ethical issues at work, costs associated with unethical behaviors, competitive advantages of being ethical, theories of human nature, individual moral development, and why good people occasionally behave unethically. Awareness of these factors is essential to thriving as a manager.

Daily Occurrence of Ethical Issues

Ethics are similar to breathing and blinking, with a slight twist. How many times do you breathe and blink in a day? We breathe and blink subconsciously, unaware that daily the average adult takes 18,000 breaths and blinks 15,000 times. Just because you are unaware of breathing and blinking this many times does not mean you don't do them.

Similarly, we tend to be unaware that every decision made during a day can be analyzed through an ethical lens and has ethical ramifications. How many times today did you think or say something was "right" or "wrong" or "good" or "bad?" Each time you did, you performed an ethical analysis.

Businesspeople create organizational problems when their business analysis is conducted without ethical analysis. The **separation thesis**, held by some business leaders, maintains that business issues can be separated from moral issues. As a result, these business leaders are

Stakeholder Any person or organization that is affected by, or could affect, an organization's goal accomplishment.

Separation thesis A theory maintaining that business issues can be separated from moral issues.

blindsided by stakeholder uproars and resultant obstacles. Business ethicists Jared Harris and R. Edward Freeman argue that “separating economic considerations and ethical considerations is impossible.”¹ They are integrative concepts that cannot be disentangled. Business decisions impact people, and whether that impact is good or bad, or right or wrong, is the domain of ethics. A decision to relocate facilities from one locality to another may be considered solely on financial concerns, but for the abandoned employees and community members, who are harmed by the decision, framing the action with an ethical lens can greatly harm the company’s reputation and bottom line through rebellious actions.

From a deep analytical perspective, all decisions are initiated by motives and result in consequences. Were our motives and intentions for making the decision good or bad, and were the consequences of our actions good or bad? Unlike breathing and blinking, which are automatic, human beings possess free will and can choose to behave ethically or unethically in any particular situation. Nonetheless, many times we make decisions as if acting subconsciously on automatic pilot. We often don’t consider the ethical nature of our decisions until we become aware that our actions harmed someone.

When an organization employs someone, that individual brings to work unique job skills and ethics. What are ethics? **Ethics** are the principles a person uses to determine whether an action is good or bad. Every stakeholder interaction can be interpreted through an ethical lens.

People experience a multitude of ethical dilemmas daily because almost every decision and action a person makes affects other people:

- Should you arrive at work early, on time, or late?
- Should you submit adequate work that meets a deadline or submit the highest-quality work possible and miss the deadline?
- Should you inform your boss about your colleague’s questionable work habits?
- Should you leave work at the designated time or cancel after-work plans and stay late to finish a project?

Ethical dilemmas are more obvious to some businesspeople than others, particularly during a time of crisis. As soon as the first U.S. citizen died from the coronavirus, some entrepreneurs sought new business opportunities to get rich quick. Obviously, the demand for hand sanitizer would soon skyrocket. Why not rent a U-Haul for 3 days, travel throughout rural Tennessee, purchase as many hand sanitizers and face masks from stores before prices increase, and then sell them at the highest prices possible on Amazon and eBay to earn huge profits? There’s nothing illegal about it—it’s just maximizing profits as a reward for your future-oriented business thinking. That’s what an entrepreneurial Tennessee man did.² For 10 years the Tennessean made a living selling hot products on Amazon and eBay. He sold his first 300 bottles of hand sanitizer on Amazon for up to \$70 each; 2,000 pandemic packs he bought at \$3.50 each sold for at least \$40 each. That was just the beginning. And he was not the only businessperson implementing this profit strategy.

Ethics The set of principles a person uses to determine whether an action is good or bad.

Although it didn't seem like an ethical issue to the Tennessean, it was an ethical issue to people wanting to protect themselves from the virus, particularly medical care workers, hospitals, police, and anyone else interacting with the public. He received hate mail and death threats. In response to a public outrage, Amazon delisted him. eBay went a step further and banned the sale of all sanitizers and masks in the United States. When Tennessee declared a state of emergency, his actions officially became illegal. The state's attorney general began investigating him for breaking the now-activated price-gouging law. He was left with 17,700 bottles of unsold hand sanitizer, which he donated to churches for distribution in hopes of avoiding fines.

Meanwhile, other businesspeople did just the opposite. They saw the pandemic as a time to care for their employees and customers.³ Home Depot froze prices on high-demand Covid-19 product categories and stopped selling face masks, which they then donated to hospitals, health care providers, and first responders. Lowe's provided employees with 14 days of emergency paid leave. With their companies facing massive layoffs, Disney board chairman Bob Iger forfeited his salary and CEO Bob Chapek took a 50% pay cut.

If you don't realize you experience a multitude of ethical issues every day—"that seems like a good/bad or right/wrong thing to do"—then you are sleepwalking through life. You are not paying attention to, or experiencing, the moral environment that surrounds you.

Ethical dilemmas are of two types, either conscious or unconscious. A *conscious* ethical dilemma occurs when you know an action is right or good, but you are tempted to do what is wrong or bad. You know you should come in to work on time today, but you are tempted to come in late, particularly since you left work late last night. Coming in late today may seem bad because coworkers are depending on you, but you think you deserve to sleep an extra hour or two. This is a conscious ethical dilemma; you are fully aware that you are making a moral choice between two competing actions. One way to resolve this ethical dilemma is to contact your boss for permission to come in late.

An *unconscious* ethical dilemma happens when you are not aware something is a moral issue, yet others might. You worked hard late last night and feel entitled to come in late, so you do. In your mind, it is not a moral issue, it's simply a personal or business decision. For a variety of reasons, you didn't even consider the negative impact your decision would have on other employees waiting for essential information they expected you to share so they could perform their early morning work. Your unanticipated lateness ruins their daily work schedules. You did not think coming in late was an ethical dilemma, but others, particularly those harmed by your behavior, did.

Some choices are obviously right or wrong, whereas others are questionable. Ethical analysis considers all aspects of an action sequence. An **action sequence** consists of the motivation behind the act, the act itself, and the consequences of the act. Acts are morally neutral. For instance, there is nothing inherently right or wrong with a manager speaking to an employee. However, the motivation leading to the act, and the consequences of the act, carry ethical weight. In this sense, actions and behaviors are surrounded, or sandwiched, by ethics.

Ethical dilemmas Situations where it is not clear whether an action is morally right or wrong, or when you know an action is right or good but are instead tempted to do what is wrong or bad.

Action sequence Consists of the motivation behind the act, the act itself, and the consequences of the act..

An ideal ethical situation is one in which a person has good motives and the act results in good consequences. When this alignment occurs, people often do not realize the act is an ethical issue, such as helping a colleague after you are caught up with your own work tasks. At the other extreme, the most unethical situation is one in which a person has bad motives and the act results in bad consequences, such as deliberately lying about a coworker's performance because you want the coworker to be undeservedly fired. Many action sequences fall between these two ethical extremes, when just motives or consequences fall short of the ideal.

Sometimes, good motives can generate bad consequences. Trying to help a colleague perform one task, for example, might distract the person from meeting an important deadline. Sometimes, bad motives can generate good consequences. An employee's selfish refusal to assist an annoying colleague may result in the colleague obtaining assistance from an even more qualified person. When evaluating these less-than-ethically-ideal situations, some people place greater ethical weight on having proper motives, such as **idealists**, whereas others place greater weight on achieving favorable outcomes, such as **consequentialists** or **pragmatists**.

Extent of Unethical Behaviors

Every organization experiences ethical and unethical behaviors. What is the extent of unethical behaviors at work? The Ethics & Compliance Initiative (ECI) has been conducting business ethics survey research since 1994. In 2019, among the 18,000 ECI worldwide survey participants, 58%, more than half, reported their organization *did not* have a strong commitment to ethical leadership.⁴ Table 1.1 summarizes five common unethical behaviors observed in business.

Even more troubling, 45% of the global respondents observed at least one of six types of major ethical misconduct during the past year. The observed misconduct rate was higher—50%—among North American respondents.⁵

Some types of misconduct were observed more often than others. Of global respondents who observed misconduct, the most common types were the following:

- Conflict of interest: 27%
- Abusive behaviors: 25%
- Violations of health and/or safety regulations: 24%
- Corruption: 19%
- Discrimination: 16%
- Sexual harassment: 13%

Among United States employees, 21% observed abusive behavior, 12% observed sexual harassment, and 12% observed discrimination.⁶ Sixty-one percent of such misconduct was considered either serious or very serious, and 62% happened on multiple occasions.

Idealist An individual who places greater ethical weight on having proper motives.

Consequentialist An individual who places greater weight on achieving favorable outcomes; also known as a **pragmatist**.

How did survey participants respond to the observed misdeeds? Thirty-four percent did not report the misconduct.⁷ Part of the reason was attributed to fear of retaliation, a reasonable fear given that 43% to 46% of those who reported sexual harassment, corruption, or discrimination experienced retaliation.

TABLE 1.1 ■ Five Common Unethical Behaviors

1. *Misuse of company time.* Altering time sheets, covering up for someone who shows up late, and conducting personal business on company time.
2. *Abusive behavior.* Using one's position or power to mistreat others and create a hostile work environment.
3. *Employee theft.* Taking products, not recording sales to friends, and manipulating expense reimbursements.
4. *Lying to employees.* Purposely misleading other employees or trying to avoid an uncomfortable interaction.
5. *Violating company Internet policies.* Surfing the Internet and checking Facebook or Twitter accounts instead of working.

The Institute of Leadership & Management surveyed United Kingdom managers about what they considered to be the most common examples of unethical behavior at their workplaces.⁸ The 1,600 manager respondents listed the following as the top misbehaviors:

- Taking shortcuts or performing low-quality work: 72%
- Lying to hide mistakes: 72%
- Bad-mouthing colleagues: 68%
- Falsely blaming others when work is not completed: 67%
- Slacking off when no one is watching: 64%
- Lying to hide a colleague's mistakes: 63%

These unethical behaviors help explain why businesses score so poorly on Gallup poll public trust surveys. Throughout the 2010s, about two-thirds of Gallup poll global respondents believed corruption was widespread in business, a sentiment held by 60% of Americans about the United States.⁹ Only 33% believed their own company would never lie or conceal information from customers, and just 29% believed their coworkers always do what's right for customers.

In a 2019 Gallup poll, respondents were asked to assess whether a profession had "very high" or "high" ethical standards. The following occupations scored thusly:¹⁰

- Nurses: 85%
- Bankers: 28%
- Business executives: 20%
- Stockbrokers: 14%

- Insurance salespeople: 13%
- Car salespeople: 11%

The low scores for business professions in annual Gallup polls can be encapsulated in the well-known quote from philosopher Rene Descartes (1596–1650): “A man is incapable of comprehending any argument that interferes with his own revenue.” The cultural perspective is that when increasing wealth conflicts with morality, the businessperson often chooses the action that increases wealth.

Even the most admired organizations can engage in ethical misconduct. In 2015 and 2016, Wells Fargo, one of the largest banks in the world, won many prestigious awards, including being the “25th Most Admired Company in the World,” “Best Bank in the U.S.,” and “Most Community-Minded Company.” Yet dating back to 2011, approximately 5,300 employees created more than 1.5 million fraudulent checking and savings accounts and 500,000 fraudulent credit cards to meet the unachievable goal of eight accounts per customer.¹¹

Profession and Industry Issues

Every profession and industry experiences unique and common ethical problems that must be managed. For instance, the economic system and interested parties rely on accountants to oversee and properly report financial statements to owners and other interested parties. Yet, despite many high-profile corporate scandals, 43% were “aware of a senior staff member making an unethical decision for a commercial result.”¹² Some accounting ethical violations are even contradictory; sometimes accountants are pressured to overreport revenue to impress investors but underreport revenue to minimize taxable income.

Claiming unearned billable hours is an issue for lawyers and consultants, as well as accountants, in their dealings with clients. To maximize profits and obtain partner status, lawyers are rewarded for charging as many hours as possible to clients. This has led some lawyers to charge clients for services not rendered; to delay concluding a case; and performing meaningless, yet billable, services.¹³ One egregious case involved a lawyer charging a client 3,500 billable hours for one year’s work, which averages out to almost 10 hours a day, 7 days a week, every week of the year.¹⁴

Public relations and sales are two professions in which employees experience significant pressure to fudge the truth. A survey of 1,700 public relations executives found that 25% of them lied on the job, and 39% exaggerated the truth.¹⁵ A survey of sales and marketing representatives revealed that 79% heard a salesperson make an unrealistic promise on a sales call, and 78% caught a competitor lying about his or her company’s products or services.

The pharmaceutical industry walks a fine line between paying physicians to share their expertise and bribing physicians to use their products. In 2019, a federal jury found Insys Therapeutics’s top executives guilty of racketeering in part for bribing doctors to prescribe their opioid products and misleading insurance companies and patients about product use.¹⁶ The company agreed to pay a \$225 million settlement. Two weeks later Insys Therapeutics declared bankruptcy.

Government agencies are not immune to unethical behavior. In the military, air force officers overseeing the launch of nuclear weapons were caught cheating on monthly proficiency exams, including tests assessing how to operate the deadly warheads.¹⁷ Several officers were also alleged to

be involved in illegal drug use. Some officers claimed these misbehaviors, along with sexual improprieties, fiscal mismanagement, drinking problems, and sleeping on the job, were rather routine.

Sexual harassment is experienced across professions and industries. For fiscal year 2018, the Equal Employment Opportunity Commission (EEOC) reported 13,055 sexual harassment submissions.¹⁸ In a review of sexual harassment research, an EEOC task force found that 60% of women surveyed say they have experienced unwanted sexual attention, sexual coercion, sexually crude conduct, or sexist comments in the workplace. Ninety percent of employees who experience sexual harassment never file a formal complaint, and 75% never complain to their employer.¹⁹ As for men, 27% were sexually harassed in a work setting.²⁰ Among industries, the highest sexual harassment occurrences are in food and service hospitality, and retail trade.

After one individual goes public about being sexually harassed, others tend to come forward. When a high-profile newswoman claimed Fox News chief executive officer (CEO) Roger Ailes had sexually harassed her, another 20 women came forward with similar claims.²¹ In the initial case, Fox settled on behalf of Ailes for \$20 million.

Many of the problems associated with managing morally imperfect employees and unethical behaviors are more, not less, prominent for small businesses. Just 4 years after new federal sentencing guidelines went into effect, 56% of the businesses prosecuted had fewer than 20 employees.²²

Operation Areas

Every operational area struggles with ethical issues. Gender and racial discrimination can occur in dealings with suppliers, employees, customers, the government, or the public at any level of the organization—board of directors, executives, middle managers, staff, or production employees—and in any department (e.g., accounting, finance, human resources, or marketing). Maintaining confidentiality, for example, is an ethical issue for executives engaged in secretive high-level negotiations, for secretaries who maintain their schedules, and for janitors who clean their offices.

Middle-level managers must balance productivity demands from superiors and job and resource limitations. In one study, 25% of middle managers admitted to having written a fraudulent internal report.²³ Usually this is done because they were directed to do so by superiors or to avoid appearing incompetent. The pressure to accomplish “more with less” is particularly stressful during economic downturns, when layoff survivors are asked to pick up the responsibilities of those dismissed without reducing their other work tasks.

Lower down the hierarchy, the most economically vulnerable employees are low-wage workers. In 2019, the U.S. Department of Labor’s Wage and Hour Division recovered a record \$322 million to resolve wage and hour claims.²⁴ Wage theft refers to not paying employees a minimum wage, overtime, or as agreed upon. This disproportionately impacts low-wage workers. An estimated 2.4 million workers in the 10 most populous states experience wage theft. At the national level, this amounts to \$15 billion in lost wages.²⁵

Starbucks strives to be a leader among ethical organizations by recognizing and responding to ethical issues at work. Its core mission is to “inspire and nurture the human spirit” among employees, customers, suppliers, and community members. Starbucks’ 2018 *Global Social Impact Report* summarizes its socially responsible outcomes in sustainability, strengthening communities, and creating opportunities, including its failures (see “Ethics in Action” for examples).²⁶

ETHICS IN ACTION

STARBUCKS' 2018 GLOBAL SOCIAL IMPACT REPORT

Leading in Sustainability	
Goal	Progress
100% ethically sourced coffee	99% of coffee (650 million pounds) was ethically sourced through C.A.F.E. (Coffee and Farmer Equity) practices
Invest \$50 million in farmer loans by 2020	Invested \$21.7 million in farmer loans in 14 countries
Train 200,000 coffee farmers by 2020	Provided free training to 52,240 coffee farmers through nine farmer support centers
Eliminate single-use straws worldwide by 2020	Engineered a new strawless lid, now 70% fewer straws used
Invest in 100% renewable energy to power operations globally by 2020	77% green energy globally, 100% in 9,000 company stores in the United States, Canada, and United Kingdom
Strengthening Communities	
Goal	Progress
66,000 hours of community service	Partners contributed 78,000 hours
On May 29, 2019, Starbucks closed 8,000 U.S. stores for 175,000 partners to participate in antibias training	
Creating Opportunities	
Goal	Progress
Employ 100,000 opportunity youths (16- to 24-year-olds out of work and not in school) by 2020	Hired 71,145 opportunity youths
42% senior leaders (senior vice presidents and above) are women	42% of senior leaders are women
100% global gender pay equity in U.S. and company-owned markets	100% pay equity achieved in the United States, Canada, and China
Graduate 25,000 partners by 2025 through Starbucks College Achievement Plan	2,400 partners earned a bachelor's degree in 2014, and 12,000 partners currently enrolled

So, what is the extent of unethical behaviors in the workplace? Contrasting views are encapsulated in the following two quotes from frontline participants:

“Morality is a job for priests, not P.R. men.”

—*Tim Bell, founder of the formerly successful, but now bankrupt, Bell Pottinger P.R. firm whose clients included dictators needing to improve their public images and whose employees had a “go anywhere, do anything” client ethos*²⁷

“We start with the shared understanding that the vast majority of businesses want to comply with the law, . . . But we also know that companies with even the best intentions can make mistakes or have a few bad actors.”

—*James McDonald, Director of Enforcement, Commodity Futures Trading Commission*²⁸

COSTS ASSOCIATED WITH UNETHICAL BEHAVIORS

Managers often underestimate the costs associated with unethical behaviors, which include legal costs, theft, recruitment and turnover costs, monitoring costs, reputation costs, and abusive treatment costs.

Legal Costs

Lawsuits are one of the most easily quantifiable costs associated with unethical behavior. Sometimes it can take years before the legal costs for unethical behavior end.

The worst financial crisis since the 1930s Great Depression began in 2007 as a result of excessive risk-taking in the subprime mortgage market. Lehman Brothers' bankruptcy created a ripple effect throughout the industry. In 2015, Standard & Poor's Financial Services (S&P) agreed to pay \$1.5 billion to the Justice Department to resolve litigation for overvaluing high-risk securities.²⁹ By 2018, financial companies had paid a staggering \$243 billion to settle mortgage-related lawsuits.³⁰ Bank of America settlements totaled \$76 billion, followed by JPMorgan Chase at \$44 billion and Citigroup at \$19 billion.³¹

Johnson & Johnson sought to maximize opioid sales in Oklahoma by making 150,000 visits to state physicians from 2000 to 2011. In a state with 3.9 million people, Oklahoma physicians wrote 18 million prescriptions from 2015 to 2018.³² This marketing plan contributed to 6,000 deaths from opioid overdose and thousands of addictions estimated to cost taxpayers and insurance companies \$893 million a year over the next 20 years. As of 2019, state lawyers reached settlements of \$572 million with Johnson & Johnson, \$270 million with Purdue Pharma, and \$85 million with Teva Pharmaceuticals. More than 500 lawsuits filed against opioid pharmaceuticals are still pending in other states. Purdue Pharma declared bankruptcy in 2019.

The mortgage and opioid settlements highlight the fallacy of employees claiming that a company should engage in morally questionable activities because “everyone else is doing it.” In this case, everyone else was heavily fined. These unanticipated expenses do not appear in initial corporate budgeting projects the year the unethical and illegal actions occur. Instead,

they accumulate over time as evidence is gathered and the legal process slowly evolves. Executive time, legal expertise, schedules, and funds must be diverted from previously planned activities to address the past mistakes.

Even if a product is legal, a company can be held liable for wrongdoing. Despite smoking being legal, tobacco companies and state attorneys general reached a \$368.5 billion settlement in 1997 for lawsuits filed to pay Medicare costs for treating sick smokers.³³

Lawsuits continue to be filed and settled every year. The Centers for Disease Control and Prevention reports that 7 million people worldwide, including 480,000 million in the United States, die from smoking.³⁴ Some cases take years of litigation with financial judgments unpredictable. In 2014, a jury awarded Judith Berger, a smoker since age 14, \$27 million, \$20 million of which was for punitive damages.³⁵ When Philip Morris won the appeal, the fine was reduced to \$3.75 million for compensatory damages. But in 2019, a U.S. district judge reinstated the original \$27 million award against Philip Morris.

Even safer legal means of nicotine intake, such as electronic cigarettes, are now subjected to lawsuits.

Employee Theft Costs

Theft represents a cost directly incurred by an organization for hiring untrustworthy employees. Employees can steal money, products, or time. Theft-related costs that are individually minimal—sending personal e-mails, conducting personal Internet searches, and making personal phone calls on company time—become substantial when aggregated across an entire workforce. For instance, the U.S. Department of Interior calculated that employee nonwork-related Internet usage cost taxpayers \$2 million and a loss of 104,221 work hours annually.³⁶

Nationwide, the U.S. Chamber of Commerce estimates that employee theft costs companies \$20 billion to \$40 billion a year. What percentage of employees are involved? Seventy-five percent, or three out of every four employees, have stolen from their employer at least once.³⁷ These thefts contribute up to 30% of business failures. The most common schemes are check tampering, payroll fraud, billing fraud, and expense padding.

The Annual Retail Theft Survey monitors theft at 20 large retail store chains representing 13,674 stores.³⁸ In 2018, 28,145 employees were caught stealing \$38 million of product.

The Association of Certified Fraud Examiners (ACFE) estimate that companies lose 5% of their annual revenue to fraud.³⁹ ACFE analyzed 2,690 fraud cases their examiners investigated in 125 countries that took place in 2016 and 2017. Accumulated losses totaled \$7.1 billion. Only 4% of the frauds were committed by someone with a prior fraud conviction. Executives were involved in 19% of the cases. Small businesses with fewer than 100 employees lost twice as much per fraud scheme than employers with more than 100 employees.

Monitoring Costs

Organizations incur monitoring costs when they employ, or do business with, unethical individuals. Once an employee has lied, he or she needs to be more closely monitored until trust is restored. Other monitoring costs include heightened supervision and increased scrutiny by

clients, auditors, or government regulators. JPMorgan Chase spent more than \$730 million over 3 years to hire 2,500 compliance employees and install other compliance features.⁴⁰

In the construction industry, despite increased electronic surveillance, theft accounts for \$1 billion in annual losses.⁴¹ The most common stolen items are small tools, appliances, wood, and heavy machinery. As a result, time and effort must be diverted for close oversight to reduce the amount of theft. But that's not all construction managers must monitor. Construction contractors list the most common unethical misconduct as artificially high bids not intended to win the contract, bid cutting, and late and short payments.⁴² The mistrust flows through the construction supply chain. Seventy-four percent of surveyed construction owners do not trust contractors, and 60% of contractors do not trust design professionals. These high levels of mistrust require extra scrutiny of key constituents.

Reputation Costs

An organization's reputation is one of its most important assets. Reputation accounts for 63% of a company's market value.⁴³ An organization's reputation can be severely damaged when lawsuits and accusations of unethical behavior appear in the media, or when customers register complaints with the Better Business Bureau.

Employees, customers, and investors consider organizational reputation when making employment and purchasing decisions. In one survey, even if unemployed, 69% of Americans would still not take a job offer from a company with an unethical reputation.⁴⁴

The most direct reputation cost is lost business. In 2016, after Wells Fargo's fraudulent customer accounts surfaced, applications for credit cards and checking accounts nosedived, the Better Business Bureau dropped the bank's accreditation, and its own headquarter city of San Francisco suspended bond contracts.⁴⁵ Wells Fargo's stock price declined by 8%, the company was fined \$185 million, and chairman and CEO John Stumpf was forced to retire, forfeiting \$41 million in pay. Four years later the public was reminded of the scandal when Stumpf was personally fined \$17.5 million and banned from the banking industry.

Organizations behaving unethically tend to underestimate the likelihood of being caught and the additional costs incurred. Many do get caught, resulting in damaged reputations and unbudgeted legal costs. One of many examples is the Volkswagen (VW) emissions scandal involving a new "clean diesel" environmentally friendly car, advertised as achieving high miles per gallon and low emissions while maintaining quick acceleration and other high-performance driving features. Engineers were unable to design the car to get both high-performance driving features and low emissions. Thus, they developed a software program that would turn on the pollution controls only when being tested by regulators.⁴⁶ From 2008 to 2015, the software, called a "defeat device," was secretly installed on about 12 million VW diesel cars sold worldwide, including 580,000 sold in the United States.

In 2014, a small team of university-based car emission test researchers in the United States detected the cheating. Volkswagen executives lied to government regulators investigating their findings. In the final "Statement of Facts" agreed to by VW, the problem was attributed company-wide, not just to a few renegade engineers. The illegal defeat device and its cover-up involved

“high-ranking executives, compliance managers, engineers, quality control experts, software specialists, and in-house lawyers.”⁴⁷ The unplanned fallout: VW’s stock price declined 30% percent, and an onslaught of lawsuits ensued. VW paid more than \$20 billion in fines and other costs as part of a settlement with the U.S. Department of Justice.⁴⁸ VW’s CEO and other managers were forced to resign, some were indicted, and VW’s reputation was severely tarnished.

Abusive Treatment Costs

Managers are mistaken if they think the costs noted earlier pertain only to the most egregious unethical behavior, such as customer fraud. Less egregious unethical behavior, such as abusive managers, can be very costly.

Abusive supervision affects approximately 13% of U.S. workers.⁴⁹ Costs in absenteeism, health care costs, and lost productivity have been estimated to be \$23.8 billion annually. Employees managed by an abusive boss respond in a variety of ways that result in additional company costs. Some employees release the abuse they incur on others, such as colleagues, subordinates, or customers requesting help. Others “get even” by stealing money and products or work less diligently when the abusive supervisor is not closely monitoring their activities. Disgruntled current and former employees express their negative views on Internet blogs and community forums, and sabotage customer relations.⁵⁰

Customers mistreated by a belligerent manager or employee also have a variety of ways to “get even.” The most prevalent predictor of health care lawsuits is not the doctor’s skills or training.⁵¹ Instead, it is the quality of the relationship between doctor and patient. Potential litigants tend not to sue doctors they like.

In France, abusive management behaviors have led to a new classification of criminal behavior called “institutional moral harassment.”⁵² In the mid-2000s, Orange, a French telecommunications company, wanted to lay off 22,000 of its 120,000 workers due to a \$50 billion debt but couldn’t because of civil servant job protections. Upper-level managers decided to make the work environment miserable so workers would voluntarily leave. Unexpectedly, 35 overstressed workers committed suicide by hanging; jumping out of windows, off bridges, and in front of trains; and setting themselves on fire. One introspective technician was given a high-pressure sales job. Feeling humiliated after a 12-hour workday with one 30-minute break, he put on a company T-shirt and hanged himself.

The company’s CEO, its second in command, and its human resources director were found guilty of institutional moral harassment, fined \$16,000, and sentenced to 4 months in jail. The company was also fined the maximum allowed under current law, \$83,000.

Recruitment and Turnover Costs

Unethical organizations incur greater costs recruiting employees, customers, suppliers, and investors, and must provide some premium to stakeholders to offset their ethical deficiencies. Once recruited, these relationships are often short-lived, resulting in high turnover among employees, customers, suppliers, and investors.

In 2018, the Work Institute estimated that 42 million people, 27% of employees, quit their jobs.⁵³ About 94% of surveyed Americans believe it is “critical” or “important” to work for an ethical company, and 33% left a company because they disagreed with its business ethics.⁵⁴ Managers and supervisors, along with nonmanagement employees, report leaving companies due to an organization’s ethical culture being weak.⁵⁵

Some leaders possess a narrow “bottom-line mentality.” Followers of these leaders are likely to support unethical pro-leader behaviors that further the interests of leaders but violate ethical norms.⁵⁶ The ethical violations include falsifying numbers for their boss, covering up for misbehaviors, withholding negative information, and misleading others. These behaviors contribute to higher turnover.

Employee Benefits News reports that costs associated with turnover are equivalent to 33% of an employee’s annual salary.⁵⁷ These costs include the following:⁵⁸

- Recruiting costs (recruiter fees, advertising)
- Interview costs (candidate travel, staff time)
- Postinterview costs (reference and screening checks, pre-employment skills tests)
- Employment costs (relocation expenses, signing bonuses)
- Training costs (training materials, staff time)

COMPETITIVE ADVANTAGES OF ETHICAL ORGANIZATIONS

Whereas unethical behavior has a negative impact on organizational operations, ethical and socially responsible behavior can have positive impacts on an organization’s bottom line. A growing amount of research on organizational performance has shifted the theoretical debate from choosing between ethical performance and financial performance to choosing ethical performance because of its contributions to financial performance.

A meta-analysis of studies examining the relationship between corporate social responsibility and corporate financial performance concluded that there was a positive causal relationship between the two, particularly in developed nations.⁵⁹ Similarly, the Great Place to Work Institute found that, compared with their peers, the 100 firms with the most ethical culture had nearly a 300% greater stock price growth.⁶⁰

How much ethics enhances financial performance depends on a wide range of issues. For instance, bankruptcy of a major customer and other market factors can overwhelm the financial benefits associated with being ethical. The linkage between social performance and financial performance is multifaceted, as outlined in Table 1.2.

If you were a *job applicant*, would you rather work for an ethical or an unethical organization?

Ethical organizations, compared with unethical organizations, are more likely to attract high-quality employees, have higher levels of employee satisfaction, and have greater employee commitment to both the organization and product or service quality.⁶¹ Ethical climate is related positively to job satisfaction and negatively to workplace isolation.

If the pay is similar, job candidates consistently choose the ethical organization rather than the unethical organization. Individuals tend to choose job offers from unethical organizations only if pay and benefits are substantially higher. In one survey, 49% of respondents would require a 50% or more pay raise if offered a position with a company that has a bad reputation.⁶² In another survey, 84% of respondents would consider leaving their current jobs for a company that has an excellent corporate reputation.⁶³

The desire to obtain employment with ethical organizations is particularly strong among Millennials, who make up half the workforce. In a Deloitte Millennial survey, “my personal values/morals” ranked first in the level of influence different factors have on their decision-making at work, with 55% reporting it had a very high degree of influence.⁶⁴ Millennials expressed a strong preference for companies that focus more on people (employees, customers, and society), products, and purpose, rather than on profits.

TABLE 1.2 ■ Competitive Advantages of Being Ethical and Trustworthy

Ethical organizations, compared with unethical organizations, are more likely to:

1. Attract and retain high-quality employees
2. Attract and retain high-quality customers
3. Attract and retain high-quality suppliers
4. Attract and retain high-quality investors
5. Earn goodwill with community members and government officials
6. Obtain greater trustworthy information for decision-making
7. Offer higher product and service quality
8. Obtain higher levels of employee productivity
9. Incur less employee theft
10. Require less employee supervision
11. Enjoy increased flexibility from stakeholders in times of emergency

If you were a *customer*, would you rather purchase products or services from an ethical or unethical organization?

A stellar ethical reputation is priceless marketing and leads to higher levels of customer satisfaction and loyalty. When product price and quality are similar, potential customers consistently choose the ethical organization over the unethical organization. A consumer survey found that 70% of Americans had not purchased a company’s product because of its questionable ethics, and 72% were willing to pay a modest premium for products and services supplied by an ethical company.⁶⁵ An unethical organization wins out over an ethical organization only if its prices are substantially lower.

Among Millennials, 36% have begun or deepened relationships with businesses because of their ethical reputation, and 37% have ended or reduced a business relationship because they considered the firm unethical.⁶⁶

If you were a *supplier*, would you rather sell your products and services to an ethical or unethical organization?

An ethical organization attracts high-quality suppliers and has higher levels of supplier satisfaction and loyalty. Potential suppliers consistently choose to sell to the ethical organization that pays a fair price rather than to the unethical organization. Suppliers depend on their customers to pay their bills on time and prefer to partner with customers they trust.

If you were an *investor*, would you rather do business with an ethical or unethical organization?

Long-term investors are attracted to ethical organizations, which leads to higher levels of investor satisfaction and loyalty. If anticipated return on investment (ROI) is similar, potential lenders and investors consistently choose the ethical organization rather than the unethical organization. Investors are drawn to organizations that adopt best practices in corporate governance.⁶⁷ They respond favorably when new accounting laws requiring financial transparency, such as the Sarbanes-Oxley Act of 2002, are legislated. In addition, banks charge lower interest rates to organizations with higher levels of institutional social performance mechanisms.⁶⁸

If you were a *community leader or government official*, would you rather interact with an ethical or unethical organization?

Ethical organizations honestly communicate with stakeholders and pay their fair share of taxes. In return, ethical organizations earn the respect of, and gain access to, community leaders and government officials. When problems arise between a company and powerful constituency groups, politicians are more likely to provide a sympathetic perspective to the company if it has a stellar community service reputation.

In addition, ethical organizations achieve a host of secondary performance benefits because they attract high-quality employees and are trusted by customers, suppliers, investors, and government officials.

Managers can make better-informed decisions when they know the information supplied by others is trustworthy. The honest flow of ideas and high levels of employee loyalty, commitment, and satisfaction in ethical organizations result in better-quality consumer products and services, higher levels of employee productivity, less employee theft, and less need for employee supervision. In addition, stakeholders are more likely to be flexible in their interactions with ethical organizations.

So, can ethical organizations achieve financial excellence? Of course they can. The more important question is how that happens, which is what this book explores, and being able to explain how it happens to owners, peers, superiors, and subordinates. “Ethical Applications” provides advice on how to frame that explanation.

Ethical Applications: Persuading Employees of the Importance of Being Ethical

Being ethical is the right thing to do, but telling that to someone who is not concerned about ethics, or is considering an unethical act, will likely fall on deaf ears. Instead, build a business case linking ethical behavior to profitability or other performance measures. That usually gets the person’s attention.

Begin by developing a list of reasons why being ethical is good for your organization's bottom line. Compelling reasons typically include customer and employee retention, lower costs, higher product quality, and employee morale. Then share a list of costs attributed to unethical behaviors, such as monitoring, reputation, turnover, and legal costs.

Given the many financial benefits associated with ethical behavior, and the many costs associated with unethical behavior, why don't all organizations excel in ethics? The core of this problem can be found in the nature of human beings and organization systems.

HUMAN NATURE

Managing ethics entails understanding human nature. Are employees, customers, and suppliers inherently selfish or altruistic; can they be trusted, or do they have to be carefully monitored? Why and how are people morally imperfect? Answers to these questions influence how managers can efficiently and effectively address ethical problems at work.

Human nature refers to the moral, psychological, and social characteristics of human beings. Philosophers, theologians, anthropologists, sociologists, and psychologists have explored and debated for centuries the moral dimensions of human nature at birth. No consensus has been achieved. Their responses, derived through both reason and faith, can be categorized into four areas: infants are born with prior knowledge of right and wrong, born good or with a moral sense, born with inherited sin, or born morally neutral.

Born With Prior Knowledge of Right and Wrong

Among the ancient Greek philosophers, Socrates and Plato theorized that individuals are born with a soul—consisting of mind, emotions, and desires—that forms an individual's inner essence.⁶⁹ The mind, filled with ideas, preexisted in a spiritual realm and joined the body at birth. With age and experience, individuals rediscover what they already knew about the world at the time of birth.

Born Good or With a Moral Sense

The second perspective on human nature tends to be grounded in religious faith.⁷⁰ Theologians in a variety of faith traditions maintain that all individuals are born in the image of God, or with a conscience, which is good. The soul is pure and sinless at birth and seeks perfect goodness. **Conscience**, in this context, is the voice of pure goodness within us. Individuals possess free will and can act in accordance with goodness or choose to do wrong. People remain connected to their original essence through righteous living. Philosopher Jean-Jacques Rousseau noted that children are born good and then learn immoral behaviors from morally corrupt adults and institutions.⁷¹

At the very least, individuals are born with a “moral sense” that directs them toward goodness. Individuals often express a “gut” feeling or moral intuition that something is right or

Human nature The moral, psychological, and social characteristics of human beings.

Conscience The voice of pure goodness within us.

wrong, although they are unable to articulate the reasoning that led to their moral conclusion. Social psychologist Jonathan Haidt attributes the moral conclusion to an individual's innate "moral sense" that is part of our psychological makeup.⁷² Our "moral sense" consists of four groups of emotions that help individuals differentiate right from wrong: (1) other-praising emotions, such as gratitude and moral awe; (2) other-condemning emotions, such as contempt, anger, and disgust; (3) other-suffering emotions, such as sympathy, compassion, and empathy; and (4) self-conscious emotions, such as guilt, shame, and embarrassment. These emotions are developed over time, inform our sense of right and wrong, and guide people along a moral path.

Psychology researcher Paul Bloom traces moral sense to birth. Within the first year of life, infants exhibit a preference for helpful behaviors, compassion, and other pleasant situations, and an aversion to mean behaviors.⁷³ Dacher Keltner claims that positive emotions, such as kindness, are at the core of human nature and part of our DNA.⁷⁴

Born With Inherited Sin

Others believe individuals are born morally imperfect, or with inherited sin. This does not mean individuals are born evil, just morally imperfect. Because of **inherited sin**, a morally damaged soul joins the body at birth and needs to be healed.

Roman Catholics and many Protestants trace inherited sin to Adam and Eve's disobedience to God's will. Saint Augustine maintained that original sin is physically transmitted through sexual intercourse, which weakens a person's will to deny evil temptations.⁷⁵ By choosing to do good, individuals restore the original essence that existed before Adam and Eve's fall from grace and reconcile with God.

Hindus and Buddhists believe a morally imperfect soul is reincarnated from one individual to another.⁷⁶ The soul of a morally imperfect person departs a body at death and then reenters the body of a newborn child. The individual currently embodying the soul is challenged to purify the moral imperfections of the individual who previously embodied the soul. The soul no longer returns to Earth after an individual achieves enlightenment, a state of oneness with God consciousness in which all desires are appropriately managed and kindness to all things has been mastered.

Born Morally Neutral

Last, some philosophers maintain that individuals are born morally neutral. Aristotle disagreed with his teacher Plato's view that infants possessed preexisting ideas and argued that at birth the mind is an "unscrubbed tablet."⁷⁷ Many centuries later, John Locke referred to this as a "**tabula rasa**," or blank slate, on which people store moral rules and knowledge based on life experiences.⁷⁸ Infants are born with moral capacities but are not preprogrammed with a set of moral principles. Their sense of morality is shaped by culture. Moral principles are learned through parental influence, experiences, and reason.

Inherited sin Belief that a morally damaged soul joins the body at birth and needs to be healed.

Tabula rasa Defined by John Locke as a blank slate, on which people store moral rules and knowledge based on life experiences.

MORAL DEVELOPMENT

In this section we examine the various theories of moral development.

Cognitive Development

Whether morally perfect, imperfect, or neutral, children are born into a particular family, neighborhood, and culture that influence children's moral judgment. Infants are born with a still-developing 3-pound brain, consisting of 100 billion neurons, which houses our thinking process and controls our central nervous system. A child's brain receives and analyzes information and formulates decisions.

With the passage of time, these decisions tend to form a pattern. One particular pattern found among children and adults is a desire to experience pleasure and avoid pain. Newborn babies cry because they feel hunger, anger, or pain and desire to be fed and comforted, which brings them pleasure.⁷⁹ Infants are also born with a sense of justice; they smile when good things occur and frown when bad things occur.⁸⁰

Parents are a child's most direct role models and shape the child's early environmental experiences. Some infants are born to kind parents who view the newborn as a gift to be cherished and fulfill a baby's physical and emotional needs. These infants tend to demonstrate emotional security, grow up trusting their surroundings, and maintain positive emotions and relationships. Other infants are emotionally neglected by their parents, who treat the newborn as a nuisance. These infants tend to become emotionally insecure, distrust their surroundings, and maintain negative emotions and relationships.

Jean Piaget (1896–1980) was among the first psychologists to outline stages of cognitive development based on patterns he observed in children, including his own.⁸¹ During the first 2 years of life, the child has an egocentric understanding of the world—the belief that what he or she sees, hears, feels, and thinks is what everyone else sees, hears, feels, and thinks.

At 18 months, children exhibit self-awareness and feelings of pride, shame, and embarrassment. By 2.5 years of age, the child understands what it means to be good or bad and by age 3 can empathize with another child's situation. As the child's conscience forms, the child becomes more capable of self-regulating emotions and behaviors. Mental scripts are developed that enable the child to generalize appropriate behaviors for different situations, such as “If someone helps me, I should say thank you,” or “When I grab other children's toys they get mad, and I should give it back instead of hitting them.”

Stages of Moral Development

Everyone has the potential to be kind or cruel to others. Why do some people make decisions that consider only their own interests, while others make decisions based on serving others?

Jean Piaget (1896–1980) One of the first psychologists to outline stages of cognitive development based on patterns he observed in children, including his own.

Harvard psychologist **Lawrence Kohlberg** (1927–1987), influenced by the writings of Piaget, sought to answer this question by analyzing how children and adults from different cultures formed moral judgments in response to a series of ethical dilemmas. The most famous is the following hypothetical situation involving Heinz stealing product from a business to save his dying wife. Through extensive research, patterns emerged in how people reasoned through these ethical dilemmas.

In Europe, a woman was near death from a special kind of cancer. There was one drug that doctors thought might save her. It was a form of radium that a druggist in the same town had recently discovered. The drug was expensive to make, but the druggist was charging 10 times what the drug cost him to make. He paid \$2,000 for the radium and charged \$20,000 for a small dose of the drug. The sick woman's husband, Heinz, went to everyone he knew to borrow the money, but he could only get together about \$10,000, which is half of what the druggist was charging. Heinz told the druggist that his wife was dying and asked him to sell it cheaper or let him pay later. But the druggist said, "No, I discovered the drug, and I'm going to make money from it." Heinz got desperate and broke into the man's store to steal the drug for his wife. Should the husband have done that?

Stages of moral development refers to an evolutionary process that describes how individuals morally reason about the rightness or wrongness of events occurring in their lives. Kohlberg and his colleagues found that people sequentially progress through a continuum of six stages of moral development, beginning with egocentric punishment avoidance and culminating at the level of applying universal ethical principles. As shown in Table 1.3, the six stages are subdivided into three levels: preconventional, conventional, and postconventional.

Each of the three levels is distinguishable by an individual's perceived relationship with society's rules and expectations. At the preconventional level, the right thing to do is that which generates personal pleasure and avoids pain. The individual is not perceived as being part of a broad community with rules and regulations. At the conventional level, the right thing to do is to be a good role model and maintain societal order. Societal roles and agreements matter a great deal to the individual. At the postconventional level, the right thing to do is to abide by abstract universal ethical principles, such as justice for everyone associated with the issue, that should be the basis of, but may conflict with, particular societal rules and regulations.

Lawrence Kohlberg (1927–1987) Harvard psychologist influenced by the writings of Jean Piaget who sought to answer the question of why some people only consider their own interests when making a decision but others make decisions based on living for the sake of others; he developed the six stages of moral development.

Stages of moral development Refers to an evolutionary process that describes how individuals morally reason about the rightness or wrongness of events that occur in their lives.

The person may stop progress at any point along these stages. An individual's level of moral reasoning is generally based on the person's age, respect for people at the next higher stage, and moral discomfort.

First, the mind becomes more capable of understanding abstract thoughts as we age. Most children under the age of 9, some adolescents, and some adults (particularly criminals) reason at the *pre-conventional* level. All pleasure-seeking pursuits are good until the pain associated with a scolding parent or authority figure outweighs the pleasure. Most adolescents and adults reason at the *conventional* level, which is why this level is called conventional or ordinary. They want others to perceive them as being good, and they understand the importance of laws for maintaining societal order and peace. Some adults, and a few adolescents, reason at the *postconventional* level. They are compelled to follow the dictates of their consciences, which are based on universal ethical principles.

Second, people predominantly apply one stage of moral reasoning, are comfortable applying lower stages, admire people one stage higher, and consider people two stages higher ethically naïve. For instance, a manager who reasons primarily at the Stage 3 “good boy–nice girl” level will occasionally justify actions based on concern for punishment and rewards, admires managers who apply “law-and-order” concerns, and thinks managers concerned about universal human rights are naïve about how businesses operate in the real world.

Third, moral discomfort plays a key factor in explaining why some adults never progress beyond the pre-conventional level (Stages 1 and 2), and most adults stop moral reasoning progress at being a good group member (Stage 3) or law-abiding citizen (Stage 4).⁸² If an individual is always content with the conclusions a particular level of moral reasoning generates, then there is little motivation to advance to the next higher sequential stage.

Fourth, some people take moral congruity very seriously, identifying strongly with the idea of having a positive and harmonious moral identity, and some do not.

TABLE 1.3 ■ Stages of Moral Development for Heinz Dilemma

Level	It Is “Right” for Heinz to Steal the Drug Because . . .	It Is “Wrong” for Heinz to Steal the Drug Because . . .
<i>Preconventional level.</i> Moral reasoning is based on what benefits the individual's needs and wants. Only my interests exist and matter.		
Stage 1: <i>Obedience and punishment orientation.</i> Right is determined by obeying an authority's rules to avoid punishment.	If Heinz lets his wife die, people will blame him for killing her.	Heinz will get caught and be punished.
Stage 2: <i>Instrumental orientation.</i> Right is determined by a selfish desire to obtain rewards and benefits from others. You should be nice to other people so that they will be nice to you.	Heinz needs his wife's companionship, and she will be grateful.	Heinz's wife will probably die soon anyway. Stealing the drug will not do him any good.

(Continued)

TABLE 1.3 ■ Stages of Moral Development for Heinz Dilemma (*Continued*)

Level	It Is “Right” for Heinz to Steal the Drug Because . . .	It Is “Wrong” for Heinz to Steal the Drug Because . . .
<i>Conventional level.</i> Moral reasoning is based on applying a social role or group membership analysis. The interests of other group members must be considered. Moral determination is based on performing good or right roles, pleasing others, and maintaining societal order.		
Stage 3: “ <i>Good boy–nice girl</i> ” orientation. Right is determined by winning the approval, and avoiding the disapproval, of others. You should be concerned about the feelings of other people and keep loyalty and trust with partners.	A good husband would do everything he can to save his wife’s life.	Heinz’s criminal behavior will bring shame and dishonor to his family.
Stage 4: “ <i>Law-and-order</i> ” orientation. Right is being a dutiful citizen who follows societal rules and maintains social order.	Heinz might be held legally responsible for not saving his wife.	Heinz is breaking the law.
<i>Postconventional level.</i> Moral reasoning is based on applying abstract universal principles. Societal and beyond societal perspectives matter. Moral determination is based on abiding by abstract principles applied to society.		
Stage 5: <i>Social contract orientation.</i> Right is determined by preserving mutually agreed-on human rights and changing unjust laws for the sake of community welfare. Individual freedom should be limited only when such freedom interferes with other people’s freedom.	The wife’s right to life is more important than the pharmacist’s profits.	We would have societal chaos if people who cannot afford products stole them.
Stage 6: <i>Universal ethical principles orientation.</i> Right is determined by following abstract universal ethical principles (such as justice, the Golden Rule, equality, and respect for life). These principles represent a universal consciousness that all humanity should follow.	Heinz’s conscience would bother him if he did not do all he could to save his wife’s life. He would want her to do the same for him.	Heinz’s conscience would bother him for stealing from the pharmacist. If he were the pharmacist, he would not want people to steal from him.

Cognitive dissonance occurs when an individual holds inconsistent or contradictory attitudes and beliefs, which creates an unpleasant state of mind. Individuals relieve this moral discomfort by reasoning at the next higher stage of moral development, which they admire. For instance, a manager could be comfortable with the conclusions generated using Stage 3 “good boy–nice girl” moral reasoning. The manager observes how other managers behave and adopts their behaviors. If other managers in the company are rewarded for selling faulty products without informing consumers of the potential dangers, then that is what a “good” manager should do.

Cognitive dissonance Occurs when an individual holds inconsistent or contradictory attitudes and beliefs, which creates an unpleasant state of mind.

But one day, the manager may become upset when a customer is seriously harmed by the product, creating cognitive dissonance. The previous moral script the manager followed—do what the other managers do—now creates psychological pain. To ease the pain, the manager might progress to the next higher stage of moral reasoning (Stage 4: “law and order”), which the manager admires, and start informing customers of the potential dangers to avoid litigation, which would generate more psychological peace.

Lies and Cheating

Managers need honest information from employees and stakeholders to achieve optimal organizational performance. Yet truthfulness is particularly challenging for many people. “Do not lie” and “do unto others as you want done to you” are two **moral imperatives**, principles compelling people to action, found in all cultures and major world religions. Despite these often-repeated moral messages, children and adults conceal and falsify the truth every day. For instance, people commonly lie about health issues, alcohol consumption, income level, weight, age, and sexual encounters. Why? They want to impress others, avoid punishment or embarrassment, protect the feelings of others, or gain an advantage.

At what age do individuals begin to lie? Children lie and deceive others as soon as they can formulate and articulate alternative strategies, which is soon after they can speak. Psychiatrist Charles Ford notes, “It is apparent that all children lie and that lying is to a large extent sanctioned, taught, and encouraged by those with whom the child comes in contact.”⁸³ If a forbidden activity is fun, children try to experience it beyond parental observation and then deny having done so if asked. As a child ages, lying to help a peer group member avoid punishment outweighs being honest with a parent, teacher, or anyone in authority.⁸⁴

Lying and cheating continue through high school. Within a year, 75% of high school students admit to copying someone’s homework and 51% to lying to a teacher. In a different study of high-achieving high school students, 80% cheated at least once during the past year.⁸⁵

Cheating patterns extend into college, where cheating is rather widespread. In a sample of nearly 2,400 respondents representing 260 business schools, approximately 52% had cheated on a test or written assignment, and more than 70% personally observed another student cheating on an exam or written assignment. A worrisome finding for businesspeople is that business school students are more likely to cheat than students with other majors.⁸⁶

Moral challenges continue into adulthood (see Table 1.4). In a classic study, Bella DePaulo and her colleagues found that adults lied on average once a day and told one lie for every five social interactions longer than 10 minutes.⁸⁷ Robert Feldman found that 60% of people lie 2 to 3 times during a 10-minute conversation.⁸⁸

Paying their fair share of taxes is particularly challenging for adults and businesses. The Internal Revenue Service (IRS) estimates there is a \$458 billion average annual difference between taxes owed and actually paid.⁸⁹ A whistleblower for the Swiss bank UBS informed authorities that 52,000 American clients hid income in offshore accounts to avoid paying

Moral imperatives Principles compelling people to action, found in all cultures and major world religions.

taxes.⁹⁰ Computer hackers obtained millions of documents from a Panamanian law firm revealing the use of shell companies by 2,400 wealthy Americans to hide their financial assets.⁹¹

People lie sometimes to obtain outcomes they have not earned or to avoid saying a harmful truth such as “your clothes make you look ugly.” Lying also serves a common social function: a defense mechanism to ward off threats to our identity as to who we think we are and how we want others to perceive us.⁹² Individuals tend not to like having their faults, imperfections, and mistakes publicly exposed. When our flaws are detected, we often deny them or cover them up to protect our reputations and self-images. Otherwise, we fear the truth about our moral flaws will result in job termination, disrespect, or some other harmful consequence. It takes a secure person with moral courage to readily admit moral faults. Situational lying remains a contentious issue (see “Up for Debate”).

TABLE 1.4 ■ The Day Americans Told the Truth: Adult Moral Challenges

In one of the most extensive studies documenting adult moral challenges, researchers surveyed thousands of people in person and through telephone interviews. The findings follow.

<ul style="list-style-type: none"> • 91% lied regularly • 35% stole office supplies • 33% lied on a job application • 31% cheated on his or her spouse 	<ul style="list-style-type: none"> • 25% cheated on income taxes • 22% lied to the boss • 22% stole from a store • 20% exaggerated an insurance claim
--	---

Source: James Patterson and Peter Kim, *The Day America Told the Truth* (New York: Prentice Hall, 1991).

UP FOR DEBATE

HONESTY AND LYING

Moral leaders encourage everyone to be truthful. Yet, on average, individuals lie once or twice a day. Sometimes individuals lie because telling the truth might cause harm to themselves or other people.

Critical Thinking Questions

1. Should individuals always tell the truth?
 - a. Yes, we should strive to always tell the truth.⁹³
 - b. No, there are times when lying is morally justified.⁹⁴
2. Why is this the right option to choose?
3. What are the ethics underlying your decision?

Moral imperfection, however, is just a small aspect of human activity. If adults lie once or twice a day, then they are honest and truthful hundreds or thousands of times every day. At any given moment, hundreds of millions of acts of kindness take place around the world.

All children may lie in certain circumstances that benefit them, but helping behaviors are also innate. Preverbal children exhibit helping behaviors before being taught rules of polite behavior by their parents.⁹⁵ By 18 months of age, toddlers exhibit **altruistic behaviors**, the deliberate pursuit of actions intended to benefit the interests or welfare of others.

In one revealing study, a researcher purposely struggled while performing ordinary tasks in front of 24 toddlers. Every time a book was “accidentally” knocked over or a towel dropped, the toddler responded in a helpful manner. By the age of 2, some children exhibit feelings of guilt when breaking someone else’s toy.⁹⁶ Preschoolers spontaneously help, without being asked, those struggling to reach for paint or trying to tie an apron.⁹⁷

These helping behaviors continue throughout adulthood. People open doors for strangers, set aside time to help friends and family members, and make philanthropic donations, sometimes anonymously.

WHY DO GOOD PEOPLE BEHAVE UNETHICALLY?

Ethics would be easy to manage if it were simply a matter of detecting and dismissing evil people. But that is not the nature of life in organizations. Most employees are good; otherwise they would be in jail rather than employed. Nonetheless, good people occasionally make ethical mistakes, which at times can be costly for an organization.

At times you might wonder why the employee you trusted so much made such an unethical decision in a particular situation. Good people occasionally behave unethically for four general reasons. First, the person may not have intended to generate the resultant unethical outcome. Second, the person may have chosen one set of values over a competing set of values. Third, the person may justify the unethical behavior based on a reason considered more compelling, such as organizational survival. Fourth, the person may choose not to prevent an unethical behavior for compelling reasons, such as fear of being fired or retaliation.

Unintended Unethical Behaviors

Unintended unethical behaviors could result from insufficient knowledge, situational ambiguity, or a misaligned management system.⁹⁸

Sometimes a person may have good motives but insufficient knowledge or awareness. For instance, the manager of a retail clothing store may generously donate unsold clothing to Goodwill to assist people in need. The used clothing is then sold in bulk by a Goodwill agent to unlicensed street vendors in San Salvador. As a result, legitimate small retailers in San Salvador, who cannot compete on price with the illegal street vendors, go bankrupt. The manager donating the clothing did not intend to bankrupt the San Salvador retailer, but that is the action sequence consequence.

Sometimes the ethics of a situation are ambiguous or complex. Assume a colleague is obviously overwhelmed by work deadlines that, if not met, could result in being terminated. Should you proactively take on some of the colleague’s work, ask others to assist, or do nothing? Assisting may seem

Altruistic behaviors The deliberate pursuit of actions intended to benefit the interests or welfare of others.

to be the ethical response. Indeed, the colleague may accuse you of being unethical for not providing the necessary assistance. However, many contextual issues must be considered before reaching a quick moral judgment. Assisting could be unethical if the work you set aside is even more important or if your assistance makes the matter worse because you lack adequate skills or knowledge.

Last, the unintended unethical behavioral outcome could result from a misaligned management system rather than the fault of a particular employee. Managers seek to maximize profit for the well-being of the company. Managers may be able to achieve higher sales and profits by using extravagant packaging and junk mail marketing. The manager does not intend to reduce the quality of life for future generations by contributing to landfill scarcity and climate change, but that is the action sequence consequence.

Choosing Between Competing Values

Sometimes the decision maker must choose between two competing values, both of which are morally appropriate. Rushworth Kidder notes, “The *really* tough choices, then, don’t center upon right versus wrong. They involve right versus right.”⁹⁹

Kidder identifies four types of ethical dilemmas associated with competing values:

- *Truth versus loyalty.* A manager may possess confidential information negatively impacting another employee. The soon-to-be affected employee asks the manager about the confidential information. Should the manager tell the truth to the employee or maintain loyalty to the company by not sharing the confidential information?
- *Individual versus community.* A company may have a scarce resource, such as a printer. Should the scarce resource be given to the one person who could most benefit from it or made available to everyone in the work group?
- *Short term versus long term.* An employee’s future progress in an organization may depend on earning an MBA degree. The employee also has two young children who want parental attention. Should the employee focus on immediate family needs or enroll in an MBA program that would financially benefit the family in the long term?
- *Justice versus mercy.* An accomplished and well-respected employee violated company policy. The company’s policy violation standards state that any employee violating the policy must be terminated. Should the manager uphold the policy and exercise justice by firing the accomplished and well-respected employee or forgive the employee’s mistake and benefit from the company’s investment in the talented employee?

All four types of ethical dilemmas represent hard choices in which an aggrieved party can claim that the decision maker has behaved unethically even though the decision maker thoughtfully made what he or she considered an ethical decision.

Intentional Unethical Behaviors

People provide a wide range of justifications for behaving unethically. The most basic reason, as suggested by Kohlberg’s theory of moral development, is to avoid punishment and receive

praise. A salesperson, for example, may declare more sales than actually achieved in a month to obtain a bonus or avoid being fired. Or the salesperson may offer an even nobler justification, such as helping the work unit or organization meet its goals. In either case, the salesperson performed a cost–benefit analysis and concluded the benefits of behaving unethically outweighed the costs.

Similar rationale can be applied by employees in any type of organization or profession. In East Lake County, Florida, the number of books checked out of the library was being monitored with the intent of removing those not used for a long time.¹⁰⁰ The library’s supervisor schemed with another employee to keep the shelves well stocked to avoid having to later repurchase discarded books. They created a fictitious library user and checked out 2,361 books under the fake patron’s name over a 9-month period, until caught. The ends, a well-stocked library, justify the means, lying about user book use.

Likewise, managers use war metaphors to justify intentional unethical behaviors. The organization is at war with its competitors, regulators, suppliers, and even customers. In this dog-eat-dog, survival-of-the-fittest environment, success requires that one must do bad to others before, or because, they do bad to you. Employees are expected to be loyal to their superior during these battles.

A survey conducted by the Society for Human Resource Management and the Ethics Resource Center found that 24% of respondents were pressured to compromise ethical standards either periodically, fairly often, or all the time.¹⁰¹ Of those feeling pressured, the top five organizational sources were the following:

1. Following the boss’s directives (experienced by 49%)
2. Meeting overly aggressive business or financial objectives (48%)
3. Helping the organization to survive (40%)
4. Meeting schedule pressures (35%)
5. Wanting to be a team player (27%)

Stanley Milgram, a professor of social psychology, conducted a series of troubling social experiments demonstrating how good people are capable of physically harming others if directed to do so by someone in authority willing to take responsibility for the act.¹⁰² Residents of New Haven, Connecticut, were recruited as participants for a learning experiment designed by the Yale University Psychology Department. They were instructed by a researcher wearing a scientific laboratory coat to administer a shock to a learner strapped in an electric chair by pressing a switch on a shock generator machine every time the learner gave an incorrect answer. The punishment level was increased by 15 volts after each subsequent wrong answer, up to a total of 450 volts. The shock generator machine’s control panel clearly labeled 195 volts as “very strong shock,” 255 volts as “intense shock,” 315 volts as “extreme intensity shock,” and 375 volts as “danger: severe shock.” If you were a participant, at what level would you stop issuing the shock?

Unknown to the participants, the learner faked being hurt by the shocks. The learner began complaining about pain from the shocks at 120 volts, demanded the experiment end after 150 volts, and let out agonizing screams at 270 volts. If a participant hesitated to administer the next level of shock following a wrong answer, the researcher directed the participant to continue. The results: 65% of the 40 participants proceeded, at 15-volt increments of increasing severity, to the maximum 450 volts of punishment despite the learner's agonizing pleas to stop. During the post-experiment debriefing, participants reported they continued to obey the experimenter's commands even though their own consciences urged them to stop physically harming the learner.

Failure to Report Unethical Behaviors

Why would a good person remain silent about unethical activities at work? In-depth interviews with 40 employees revealed that 85% of them had not raised an important issue or concern to their bosses on at least one occasion. The top reasons for not informing a manager about unethical behaviors were the following:¹⁰³

- Fear of being labeled or viewed negatively by others, such as being considered a troublemaker, tattletale, or complainer
- Fear of damaging relationships with the person committing the unethical act
- Fear of retaliation or punishment from the person committing the unethical act
- Fear of negatively affecting the life of the person committing the unethical act
- Fear of being blamed for the problem
- Belief that management would not act on the issue if informed

Failure to report unethical behavior can be costly in lives as well as money. In 2001, General Motors (GM) engineers first detected an ignition switch defect during preproduction testing of the Saturn Ion and recognized the same defect 3 years later in the Chevrolet Cobalt.¹⁰⁴ An engineer recommended redesigning the switch in 2005, but upper management advised against it because of costs. A few months later, the first fatality associated with the defect occurred. Without informing management, the switch engineer then redesigned the ignition switch.

Although the engineer's unapproved change was admirable, defective models remained on the road. By 2013, GM attributed at least 13 deaths and 31 crashes to the ignition switch defect. In 2014, a few weeks after a new CEO was hired, GM finally notified government regulators that the defect existed in 619,122 cars. A series of recalls were initiated, totaling 30 million cars worldwide. GM was initially fined \$35 million for the delay in reporting the problem. Litigation by victims led to GM setting aside \$625 million in victim compensation. By 2016, GM had paid more than \$6 billion in fines, lawsuit settlements, and recall costs, with additional litigation costs mounting.¹⁰⁵ When questioned by the media about those who died, the engineer broke down and cried, and then defended his actions by saying, "I did my job the best I could."¹⁰⁶

So, Why Be Moral?

In this chapter you read about Starbucks executives deciding to close stores for antibiotics training, and achieving 100% renewable energy in the United States, Canada, and United Kingdom. You also read about Orange executives deciding to create a toxic work environment to encourage employees to quit, and it led to 35 suicides. On a less profound scale, you read about employees choosing to be honest and others choosing to lie.

There always seems to be a small group of individuals seeking to make as much money as they can by behaving unethically. Some of them become billionaires, such as Travis Kalanick, Uber's cofounder and former CEO and chairman of the board.¹⁰⁷ A highly competitive workaholic, Kalanick created an outcome-based meritocratic work environment, unconcerned about lies, abusive behaviors, sexual harassment, and other workplace process factors. Kalanick and other employees unethically and blatantly skirted and violated the law.

Being kind or cruel to others is an individual choice. Why choose being kind over cruel, honest over lying, and ethical over unethical?

Earlier we addressed this issue at the organizational level. In the long-term, ethical companies financially outperform unethical organizations. Ethical organizations attract ethical and loyal employees, customers, suppliers, and investors. They earn community goodwill and increased flexibility from stakeholders. Ethical organizations also have higher product and service quality and productivity, fewer employee theft incidents, and less turnover and legal costs. These are all organizational benefits for choosing to be ethical.

But what about at the individual level? What are the personal benefits of being moral?

First and foremost, choosing to be moral creates a tremendous amount of inner peace and self-respect. Your conscience is more at ease by following the inner voice telling you to do the right thing, rather than debating yourself, choosing what is wrong, feeling guilty about the choice, feeling shame when exposed, and internalizing bad memories.

Second, choosing to be moral generates positive relationships with other people. Others can trust you because they know you will treat them as you would want to be treated, respect them, keep your promises, and be fair. They do not have to worry about you backstabbing or sabotaging them. They can depend on you when things go wrong. And they often reciprocate the good deed.

Third, choosing to be moral enables individual freedom and civil society to exist. Moral people can be trusted with freedom and to not abuse their freedom to the detriment of others. Being moral connects you with society's long historical march toward creating a better world. You form bonds with others who have been on, or are on, a common mission to give their best efforts in fostering more humane families, communities, organizations, and nations.

There will be bumps in the road. Your conscience may encourage you to make a politically unwise decision that can lead to a demotion or dismissal. You will fail at times, give in to unethical peer pressure, or justify doing something unethical for the good of the organization or job security. And your conscience will remind you of these momentary failures until you forgive yourself or others forgive you.

Ultimately, each decision you make shapes your character and identity, defining who you are to yourself and others. Each decision you make builds your reputation, which follows you

wherever you go. At the end of the day or year, or at the end of your career or life, the decisions you make will contribute to a peaceful or turbulent mind.

By implementing the best practices for designing and managing ethical organizations presented in this book, you will generate inner peace, a more humane business system, and enhanced organizational profits.

SUMMARY

Organizations are complex human endeavors. Individuals have a dual nature. People are primarily honest but also lie when it is beneficial. They care primarily for their own welfare but also for the welfare of others. They are kind to others but can also be cruel at times. In a general sense, individuals seek to experience pleasure and avoid pain; have a sense of right and wrong; and are influenced by reasons and emotions, their conscience, and their peers. Nobody is morally perfect, although some people are more ethical than others.

We have all experienced high-integrity managers and owners who have earned our trust, be it the local plumber who does high-quality work at reasonable prices or a corporate executive who constructively responds to customer complaints. We reward them with our loyalty.

We have also all experienced untrustworthy phone solicitors, Internet scammers, or a business executive or manager who lied to us or treated us poorly. This latter group's behaviors are highlighted in daily, weekly, monthly, and annual media exposes of corrupt businesspeople.

Managers typically underestimate the prevalence of work-related ethical problems and the financial costs associated with unethical behaviors. Recognizing that all humans are morally flawed may seem slightly depressing. But recognizing human frailty enables managers to make informed plans that are more likely to succeed. Appropriately managing ethics can create many competitive advantages that lead to superior organizational and financial performance.

KEY WORDS

Action sequence
Altruistic behaviors
Cognitive dissonance
Conscience
Consequentialist
Ethical dilemmas
Ethics
Human nature
Idealist
Inherited sin

Jean Piaget
Lawrence Kohlberg
Moral imperatives
Pragmatist
Separation thesis
Stages of moral development
Stakeholder
Tabula rasa
Well-managed organization

CHAPTER QUESTIONS

1. What are the most common types of unethical behaviors in organizations?
2. How do unethical behaviors increase organizational costs?
3. What are the competitive advantages of creating and sustaining an ethical organization?
4. What are the four beliefs about human nature as related to ethics at the time of birth?
5. What are the six stages of moral development?
6. Why do good people occasionally behave unethically, and why should you be moral?

Do not copy, post, or distribute

Do not copy, post, or distribute