Chapter 1

Ethics and Business

Good people do not need laws to tell them to act justly, while bad people will find a way around the laws.

*Plato*

It is difficult to get a man to understand something when his salary depends upon his not understanding it.

*Upton Sinclair*
During the early evening hours of December 11, 1995, a fire broke out in a textile mill in Lawrence, Massachusetts. By morning, the fire had destroyed most of Malden Mills, the manufacturer of Polartec fabric. The fire seemed a disaster to the company, its employees, its customers, and the surrounding communities.

Malden Mills was a family-owned business, founded in 1906 and run by the founder’s grandson Aaron Feuerstein. Polartec is a high-quality fabric well known for its use in the outdoor apparel featured by such popular companies as L.L. Bean, Lands’ End, REI, J. Crew, and Eddie Bauer. The disaster promised many headaches for Malden Mills and for the numerous businesses that depend on its products.

But the fire also was a disaster for an entire community. The towns surrounding the Malden Mills plant have long been home to textile manufacturing. But the industry effectively died during the middle decades of the twentieth century when outdated factories and increasing labor costs led many companies to abandon the area and relocate, first to the nonunionized South, and later to foreign countries such as Mexico and Taiwan. As happened in many northern manufacturing towns, the loss of major industries, along with their jobs and tax base, began a long period of economic decline from which many have never recovered. Malden Mills was the last major textile manufacturer in town, and with 2,400 employees it supplied the economic lifeblood for the surrounding communities. With both its payroll and taxes, Malden Mills contributed approximately $100 million a year into the local economy.

As CEO and president, Aaron Feuerstein faced some major decisions. He could have used the fire as an opportunity to follow his local competitors and relocate to a more economically attractive area. He certainly could have found a location with lower taxes and cheaper labor and thus have maximized his earning potential. He could have simply taken the insurance money and decided not to reopen at all. Instead, as the fire was still smoldering, Feuerstein pledged to rebuild his plant at the same location and keep the jobs in the local community. But even more surprising, he promised to continue paying his employees and extend their medical coverage until they could come back to work.

What do you think of Feuerstein’s decision? What would you have done had you been in his position?

What facts would be helpful as you make your judgments about Feuerstein?

How many different ethical values are involved in this situation? What kind of man is Feuerstein? How would you describe his actions after the fire? Can you describe the man and his actions without using ethical or evaluative words?

Whose interests should Feuerstein consider in making this decision? How many different people were affected by the fire and the decision?

What other options were available for Feuerstein? How would these alternatives have affected the other people involved?

Were Feuerstein’s actions charitable, or was this something he had a duty or obligation to do? What is the difference between acts of charity and obligatory acts?
Chapter Objectives

After reading this chapter, you will be able to:

1. Explain why ethics is important in the business environment.
2. Explain the nature of business ethics as an academic discipline.
3. Distinguish the ethics of personal integrity from the ethics of social responsibility.
4. Distinguish ethical norms and values from other business-related norms and values.
5. Distinguish legal responsibilities from ethical responsibilities.
7. Distinguish ethical decision making from other practical decision situations.

Introduction: Making the Case for Business Ethics

From the time Enron Corporation collapsed in 2001, business ethics has seldom strayed from the front pages of the press. The list of corporations and business leaders that have been involved with legal and ethical wrongdoing is, sadly, incredibly long. Reflect for a moment on the businesses that have been involved in recent scandals: Enron, WorldCom, Tyco, Adelphia, Cendant, Rite Aid, Sunbeam, Waste Management, HealthSouth, Global Crossing, Arthur Andersen, Ernst & Young, Imclone, KPMG, JPMorgan, Merrill Lynch, Morgan Stanley, Citigroup Salomon Smith Barney, Marsh & McLennan, Credit Suisse First Boston, and even the New York Stock Exchange itself. Individuals implicated in ethical scandals include Martha Stewart, Kenneth Lay, Jeffrey Skilling, Andrew Fastow, Dennis Kozlowski, John J. Rigas, Richard M. Scrushy, Samuel Waksal, Richard Grasso, and Bernard Ebbers. Beyond these well-known scandals, consumer boycotts based on allegations of unethical conduct have targeted such well-known firms as Nike, McDonald’s, Home Depot, Gap, Shell Oil, Levi-Strauss, Donna Karen, Kmart, and Wal-Mart.

This chapter will introduce business ethics as a process of responsible decision making. Simply put, the scandals and ruin experienced by all the institutions and every one of the individuals just mentioned were brought about by ethical failures. This text provides a decision-making model that, we hope, can help individuals understand such failures and avoid future business and personal tragedies. As an introduction to that decision-making model, this chapter reflects on the nature of ethics and business.

Ethical decision making in business is not limited to the type of major corporate decisions with dramatic social consequences listed above. At some point every worker, and certainly everyone in a managerial role, will be faced with an issue that will require ethical decision making. Not every decision can be covered by economic, legal, or company rules and regulations. More often than not,
responsible decision making must rely on the personal values and principles of the individuals involved. Individuals will have to decide for themselves what type of person they want to be.

At other times, of course, decisions will involve significant general policy issues that affect entire organizations, as happened in all the well-known corporate scandals and in the Malden Mills case described at the start of this chapter. The managerial role especially involves decision making that establishes organizational precedents and has organizational and social consequences. Hence, both of these types of situations—the personal and the organizational—are reflected in the title of this book: *Business Ethics: Decision Making for Personal Integrity and Social Responsibility.*

As recently as the mid-1990s, articles in such major publications as *The Wall Street Journal*, the *Harvard Business Review*, and *U.S. News and World Report* questioned the legitimacy and value of teaching classes in business ethics. Few disciplines face the type of skepticism that commonly confronted courses in business ethics. Many students believed that, like “jumbo-shrimp,” “business ethics” was an oxymoron. Many also viewed ethics as a mixture of sentimentality and personal opinion that would interfere with the efficient functioning of business. After all, who is to say what’s right or wrong?

Throughout the 1980s and 1990s, this skeptical attitude was as common among business practitioners as it was among students. But this simply is no longer the case in contemporary business. The questions today are less about why or should ethics be a part of business, than they are about which values and principles should guide business decisions and how ethics should be integrated within business. Students unfamiliar with the basic concepts and categories of ethics will find themselves as unprepared for careers in business as students who are unfamiliar with accounting and finance. Indeed, it is fair to say that students will not be fully prepared even within fields such as accounting, finance, human resource management, marketing, and management unless they are familiar with the ethical issues that arise within those specific fields. You simply will not be prepared for a career in accounting, finance, or any area of business if you are unfamiliar with the ethical issues that commonly occur in these fields.

To understand the origins of this change, consider the range of people who were harmed by the collapse of Enron. Stockholders lost over $1 billion in stock value. Thousands of employees lost their jobs, their retirement funds, and their health care benefits. Consumers in California suffered from energy shortages and blackouts that were caused by Enron’s manipulation of the market. Hundreds of businesses that worked with Enron as suppliers suffered economic loss with the loss of a large client. Enron’s accounting firm, Arthur Andersen, went out of business as a direct result. The wider Houston community was also hurt by the loss of a major employer and community benefactor. Families of employees, investors, and suppliers were also hurt. Many of the individuals directly involved will themselves suffer criminal and civil punishment, including prison sentences for some. Indeed, it is hard to imagine anyone who was even loosely affiliated with Enron.
who was not harmed as a result of the ethical failings there. Multiply that harm by the dozens of other companies implicated in similar scandals and you get an idea of why ethics is no longer dismissed as irrelevant. The consequences of unethical behavior and unethical business institutions are too serious for too many people to be ignored.

This description of the consequences of the Enron collapse, along with the opening description of the Malden Mills case, demonstrates the significant impacts that business decisions can have on a very wide range of people. Both cases dramatically affected the lives of thousands of people: employees, stockholders, management, suppliers, customers, and surrounding communities. For better or for worse, the decisions a business firm makes will affect many more people than just the decision maker. Ethically responsible business decision making therefore must move beyond a narrow concern with stockholders to consider the impact that decisions will have on a wide range of stakeholders. In a general sense, a business stakeholder will be anyone affected, for better or worse, by decisions made within the firm.

The preceding Reality Check describes some legal requirements that have been created since the Enron fiasco. Beyond these specific legal obligations, contemporary business managers have many other reasons to be concerned with ethical issues. Unethical behavior not only creates legal risks for a business, it creates financial and marketing risks as well. Managing these risks requires managers and executives to remain vigilant about their company’s ethics. It is now clearer than ever that a company can lose in the marketplace, it can go out of business, and its employees can go to jail if no one is paying attention to the ethical standards of the firm. A firm’s ethical reputation can provide a competitive advantage or disadvantage in the marketplace and with customers, suppliers, and employees. The consumer boycotts of such well-known firms as Nike, McDonald’s, Home

### Reality Check

**Why Be Ethical? Because the Law Requires It**

Today, business executives have many reasons to be concerned with the ethical standards of their organizations. Perhaps the most straightforward reason is that the law requires it. In 2002, the U.S. Congress passed the Sarbanes-Oxley Act to address the wave of corporate and accounting scandals. Section 406 of that law, “Code of Ethics for Senior Financial Officers,” requires that corporations have a Code of Ethics “applicable to its principal financial officer and comptroller or principal accounting officer, or persons performing similar functions.” The Code must include standards that promote:

1. **Honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships.**
2. **Full, fair, accurate, timely, and understandable disclosure in the periodic reports required to be filed by the issuer.**
3. **Compliance with applicable governmental rules and regulations.**
Depot, and Wal-Mart mentioned previously give even the most skeptical business leader reason to pay attention to ethics. Managing ethically can also pay significant dividends in organizational structure and efficiency. Trust, loyalty, commitment, creativity, and initiative are just some of the organizational benefits that are more likely to flourish within ethically stable and credible organizations (see the Reality Check above).

For business students, the need to study ethics should be as clear as the need to study the other subfields of business education. Without this background, students simply will be unprepared for a career in contemporary business. But even for students not anticipating a career in business management or business administration, familiarity with business ethics is just as crucial. After all, it was not only the managers at Enron who suffered because of their ethical lapses. Our lives as employees, as consumers, and as citizens are affected by decisions made within business institutions, and therefore everyone has good reasons for being concerned with the ethics of those decision makers.

The case for business ethics is by now clear and persuasive. Business must take ethics into account and integrate ethics into its organizational structure. Students need to study business ethics. But what does this mean? What is “ethics,” and what is the point of a class in business ethics?

### Business Ethics as Ethical Decision Making

As the title of this book suggests, our approach to business ethics will emphasize ethical decision making. No book can magically create ethically responsible people or change behavior in any direct way. But students can learn and practice responsible ways of thinking and deliberating. We assume decisions that follow from a process of thoughtful and conscientious reasoning will be more responsible and ethical decisions. In other words, responsible decision making and deliberation will result in more responsible behavior.

So what is the point of a business ethics course? On one hand, *ethics* refers to an academic discipline with a centuries-old history, and we might expect knowledge
about this history to be among the primary goals of a class in ethics. Thus, in an ethics course, students might be expected to learn about the great ethicists of history such as Aristotle, John Stuart Mill, and Immanuel Kant. As in many other courses, this approach to ethics would focus on the informational content of the class.

Yet, according to some observers, learning about ethical theories and gaining knowledge about the history of ethics is beside the point. Many people, ranging from businesses looking to hire college graduates to business students and teachers themselves, expect an ethics class to address ethical behavior, not just information and knowledge about ethics. After all, shouldn’t an ethics class help prevent future Enrons? Ethics refers not only to an academic discipline, but to that arena of human life studied by this academic discipline, namely, how human beings should properly live their lives.

Yet, a caution about influencing behavior within a classroom is appropriate. Part of the hesitation about teaching ethics involves the potential for abuse; expecting teachers to influence behavior may be viewed as permission for teachers to impose their own views on students. Many believe that teachers should remain value-neutral in the classroom and respect a student’s own views. Another part of this concern is that the line between motivating students and manipulating students is a narrow one. There are many ways to influence someone’s behavior, including threats, guilt, pressure, bullying, and intimidation. Some of the executives involved in the worst of the recent corporate scandals were very good at using some of these means to motivate the people who worked for them. Presumably, none of these approaches belong in a college classroom, and especially not in an ethical classroom.

But not all forms of influencing behavior raise such concerns. There is a major difference between manipulating someone and persuading someone, between threats and reasons. This textbook resolves the tension between knowledge and behavior by emphasizing ethical judgment, ethical deliberation, ethical decision making. We agree with those who believe that an ethics class should strive to produce more ethical behavior among the students who enroll. But we believe that the only academically and ethically legitimate way to do this is through careful and reasoned decision making. Our fundamental assumption is that a process of rational decision making, a process that involves careful thought and deliberation, can and will result in behavior that is both more reasonable and more ethical.

Perhaps this view is not surprising after all. Consider any course within a business school curriculum. Doesn’t a management course aim to create better managers? Wouldn’t we judge as a failure any finance or accounting course that denied a connection between the course material and financial or accounting practice? Every course in a business school assumes a connection between what is taught in the classroom and appropriate business behavior. Classes in management, accounting, finance, and marketing all aim to influence students’ behavior. All assume that the knowledge and reasoning skills learned in the classroom will lead to better decision making and therefore better behavior within a business context. A business ethics class is no different.

While few teachers think that it is our role to tell students the right answers and proclaim what they ought to think and how they ought to live, fewer still think that
there should be no connection between knowledge and behavior. Our role should not be to preach ethical dogma to a passive audience, but to treat students as active learners and engage them in an active process of thinking, questioning, and deliberating. Taking Socrates as our model, philosophical ethics rejects the view that passive obedience to authority or the simple acceptance of customary norms is an adequate ethical perspective. Teaching ethics must, in this view, involve students thinking for themselves. The decision-making model that will be presented in the next chapter offers one such process of ethical analysis, deliberation, and reasoning.

**Business Ethics as Personal Integrity and Social Responsibility**

Another aspect of ethical behavior that deserves mention is the fact that social circumstances also have a significant influence over behavior. An individual may have carefully thought through a situation and decided what is right and may be motivated to act accordingly, but the corporate or social context surrounding the individual may create serious barriers to do so. As individuals, we need to recognize that our social environment will greatly influence the range of options that are open to us and can significantly influence our behavior. Otherwise good people can, in the wrong circumstances, do bad things and less ethically motivated individuals can, in the right circumstances, do the right thing. Business leaders therefore have a responsibility for the business environment, what we shall later refer to as the corporate culture, to encourage or discourage ethical behavior. Ethical business leadership is exactly this skill: to create the circumstances in which good people are able to do good, and bad people are prevented from doing bad.

Again, the Enron case provides an example. Sherron Watkins, an Enron vice president, seemed to understand fully the corruption and deception that was occurring within the company, and she took some small steps to address the problems. But when it became clear that her boss might use her concerns against her, she backed off. So, too, with some of the Arthur Andersen auditors involved. When some individuals raised concerns about Enron’s accounting practices, their supervisors pointed out that the $100 million annual revenues generated by the Enron account provided good reasons to back off. The Decision Point that follows exemplifies the culture present at Enron during the heat of its downfall.

At its most basic level, ethics is concerned with how we act and how we live our lives. Ethics involves what is perhaps the most monumental question any human being can ask: How *should* we live? Ethics is, in this sense, *practical*, having to do with how we act, choose, behave, do things. Philosophers often emphasize that ethics is *normative*, in that it deals with our reasoning about how we *should* act. Social sciences such as psychology and sociology also examine human decision making and actions, but these sciences are *descriptive* rather than normative. They provide an account of how and why people *do* act the way they do; as a normative discipline, ethics seeks an account of how and why people *should* act, rather than how they *do* act.
Following is a portion of the famous memo that Sherron Watkins, an Enron vice president, sent to CEO Kenneth Lay as the Enron scandal began to unfold. As a result of this memo, Watkins became famous as the Enron “whistleblower.”

Has Enron become a risky place to work? For those of us who didn’t get rich over the last few years, can we afford to stay? Skilling’s [former Enron CEO Jeffrey Skilling] abrupt departure will raise suspicions of accounting improprieties and valuation issues . . . . The spotlight will be on us, the market just can’t accept that Skilling is leaving his dream job . . . . It sure looks to the layman on the street that we are hiding losses in a related company and will compensate that company with Enron stock in the future . . . .

I am incredibly nervous that we will implode in a wave of accounting scandals. My eight years of Enron work history will be worth nothing on my résumé, the business world will consider the past successes as nothing but an elaborate accounting hoax.

Skilling is resigning now for “personal reasons” but I would think he wasn’t having fun, looked down the road and knew this stuff was unfixable and would rather abandon ship now than resign in shame in two years.

Is there a way our accounting gurus can unwind these deals now? I have thought and thought about a way to do this, but I keep bumping into one big problem—we booked the Condor and Raptor deals in 1999 and 2000, we enjoyed wonderfully high stock price, many executives sold stock, we then try and reverse or fix the deals in 2001, and it’s a bit like robbing the bank in one year and trying to pay it back two years later. Nice try, but investors were hurt, they bought at $70 and $80 a share looking for $120 a share and now they’re at $38 or worse. We are under too much scrutiny and there are probably one or two disgruntled “redeployed” employees who know enough about the “funny” accounting to get us in trouble . . . . I realize that we have had a lot of smart people looking at this and a lot of accountants including AA & Co. [Arthur Andersen] have blessed the accounting treatment. None of that will protect Enron if these transactions are ever disclosed in the bright light of day. (Please review the late 90’s problems of Waste Management [news/quote]—where AA paid $130 million plus in litigation re questionable accounting practices . . . .

I firmly believe that executive management of the company must . . . decide one of two courses of action: 1. The probability of discovery is low enough and the estimated damage too great; therefore we find a way to quietly and quickly reverse, unwind, write down these positions/transactions. 2. The probability of discovery is too great, the estimated damages to the company too great; therefore, we must quantify, develop damage containment plans and disclose . . . . I have heard one manager-level employee from the principal investments group say, “I know it would be devastating to all of us, but I wish we would get caught. We’re such a crooked company.” These people know and see a lot.

After the collapse of Enron, Watkins was featured on the cover of Time magazine and honored as a corporate whistleblower, despite the fact that she never shared these concerns with anyone other than Kenneth Lay. Was Watkins an ethical hero in taking these steps?

- What facts would you want to know before making a judgment about Watkins?
- What ethical issues does this situation raise?

(continued)
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How should we live? This fundamental question of ethics can be interpreted in two ways. “We” can mean each one of us individually, or it might mean all of us collectively. In the first sense, this is a question about how I should live my life, how I should act, what I should do, what kind of person I should be. This meaning of ethics is sometimes referred to as morality, and it is the aspect of ethics that we refer to by the phrase “personal integrity.” There will be many times within a business setting where an individual will need to step back and ask: What should I do? How should I act?

In the second sense, “How should we live?” refers to how we live together in a community. This is a question about how a society and social institutions such as corporations ought to be structured and about how we ought to live together. This area is sometimes referred to as social ethics and it raises questions of justice, public policy, law, civic virtues, organizational structure, and political philosophy. In this sense, business ethics is concerned with how business institutions ought to be structured, about corporate social responsibility, and about making decisions that will impact many people other than the individual decision maker. This aspect of business ethics asks us to examine business institutions from a social rather than an individual perspective. We refer to this broader social aspect of ethics as decision making for social responsibility.

In essence, managerial decision making will always involve both aspects of ethics. Each decision a business manager makes not only involves a personal decision, but also involves making a decision on behalf of, and in the name of, an organization that exists within a particular social, legal, and political environment. Thus, our book’s title makes reference to both aspects of business ethics. Within a business setting, individuals will constantly be asked to make decisions affecting both their own personal integrity and their social responsibilities.

Expressed in terms of how we should live, the major reason to study ethics becomes clear. Whether we explicitly examine these questions or not, each and every one of us answers them every day in the course of living our lives. Whatever decisions business managers make, they will have taken a stand on ethical issues, at least.

• Besides Kenneth Lay, who else might have had an interest in hearing from Watkins? Who else might have had a right to be informed? Did Watkins have a responsibility to anyone other than Lay?
• Other than her informing Lay, what other alternatives might have been open to Watkins?
• What might the consequences of each of these alternatives had been?
• From this section of the memo, how would you characterize Watkins’ motivation? What factors seem to have motivated her to act?
• If you were Ken Lay and had received the memo, what options for next steps might you have perceived? Why might you have chosen one option over another?
• Do you think Watkins should have taken her concerns beyond Kenneth Lay to outside legal authorities?

(concluded)
implicitly. The actions each one of us takes and the lives we lead give very practical and unavoidable answers to fundamental ethical questions. Our only real choice is whether we answer them deliberately or unconsciously. Philosophical ethics simply asks us to step back from these unavoidable everyday decisions to examine and evaluate them. Thus, Socrates gave the philosophical answer to why you should study ethics over 2000 years ago: “The unexamined life is not worth living.”

To distinguish ethics from other practical decisions faced within business, consider two approaches to the Malden Mills scenario that opened this chapter. This case could just as well be examined in a management, human resources, or organizational behavior class as in an ethics class. The more social-scientific approach common in management or business administration classes would examine the situation and the decision by asking questions such as, What factors led to one decision rather than another? Why did this manager act the way he did?

A second approach to Malden Mills, from the perspective of ethics, steps back from the facts of the situation to raise such questions as, What should the manager do? What rights and responsibilities are involved? What advice ought Feuerstein’s tax accountant or human resource manager offer? What good will come from this situation? Is Feuerstein being fair, just, virtuous, kind, loyal, trustworthy? This normative approach to business is at the center of business ethics. Ethical decision making involves the basic categories, concepts, and language of ethics: shoulds, oughts, rights and responsibilities, goodness, fairness, justice, virtue, kindness, loyalty, trustworthiness, honesty, and the like.

To say that ethics is a normative discipline is to say that it deals with norms, those standards of appropriate and proper (or “normal”) behavior. Norms establish the guidelines or standards for determining what we should do, how we should act, what type of person we should be. Another way of expressing this point is to say that norms appeal to certain values that would be promoted or attained by acting in a certain way. Normative disciplines presuppose some underlying values.

But to say that ethics is a normative discipline is not to say that all normative disciplines involve ethics. After all, isn’t business management and business
administration itself normative? Aren’t there norms for business managers that presuppose a set of business values? One could add accounting and auditing to this list, as well as economics, finance, politics, and the law. Each of these disciplines appeals to a set of values to establish the norms of appropriate behavior within each field.

These examples suggest that there are many different types of norms and values. In general, we can think of values as those beliefs that incline us to act or to choose one way rather than another. Thus, the value that I place on an education leads me to study rather than play video games. I believe that education is more worthy, or valuable, than playing games. I choose to spend my money on groceries rather than on a vacation because I value food more than relaxation. A company’s core values, for example, are those beliefs and principles that provide the ultimate guide in its decision making.

Understood in this way, many different types of values can be recognized: financial, religious, legal, historical, nutritional, political, scientific, and aesthetic. Individuals can have their own personal values and, importantly, institutions also have values. Talk of a corporation’s “culture” is a way of saying that a corporation has a set of identifiable values that establish the expectations for what is “normal” within that firm. These norms guide employees, implicitly more often than not, to behave in ways that the firm values and finds worthy. One important implication of this, of course, is that an individual or a corporation can have a set of unethical values. The corporate culture at Enron, for example, seems to have been committed to pushing the envelope of legality as far as possible to get away with as much as possible in pursuit of as much money as possible. Values? Yes. Ethical values? No.

One way to distinguish these various types of values is in terms of the ends they serve. Financial values serve monetary ends, religious values serve spiritual ends, aesthetic values serve the end of beauty, legal values serve law, order, and justice, and so forth. Different types of values are distinguished by the various ends served by those acts and choices. So, how are ethical values to be distinguished from these other types of values? What ends does ethics serve?

Values, in general, were earlier described as those beliefs that incline us to act or choose in one way rather than another. Consider again the harms attributed to the ethical failures at Enron. Thousands of innocent people were hurt by the decisions made by some individuals seeking their own financial and egotistical aggrandizement. This example reveals two important elements of ethical values. First, ethical values serve the ends of human well-being. Acts and choices that aim to promote human welfare are acts and choices based on ethical values. Controversy may arise when we try to specify more precisely what is involved in human well-being, but we can start with some general observations. Happiness certainly is a part of it, as is respect, dignity, integrity, and meaning. Freedom and autonomy surely seem a part of human well-being, as do companionship and health.

Second, the well-being promoted by ethical values is not a personal and selfish well-being. After all, the Enron scandal resulted from many individuals seeking to promote their own well-being. Ethics requires that the promotion of human well-being be done impartially. From the perspective of ethics, no one person’s welfare is to count as more worthy than any other’s. Ethical acts and choices should be acceptable and reasonable from all relevant points of view. Thus, we can offer an
initial characterization of ethics and ethical values. Ethical values are those beliefs and principles that impartially promote human well-being.

**Ethics and the Law**

Any discussion of norms and standards of proper behavior would be incomplete without considering the law. Deciding what one *should do* in business situations often requires reflection on what the law requires, expects, or permits. The law provides a very important guide to ethical decision making, and this text will integrate legal considerations throughout. But legal norms and ethical norms are not identical nor do they always agree. Some ethical requirements, such as treating one’s employees with respect, are not legally required though they may be ethically warranted. Conversely, some actions that can be legally allowed, such as firing an employee for no reason, would fail ethical standards.

A common view, perhaps more common prior to the scandals of recent years than after, holds that a business fulfills its social responsibility simply by obeying the law. From this perspective, an ethically responsible business decision is merely one that complies with the law; there is no responsibility to do anything further. Individual businesses may decide to go beyond the legal minimum, as when a business supports the local arts, but such choices are voluntary. A good deal of management literature on corporate social responsibility centers on this approach, contending that ethics requires obedience to the law; anything beyond that is a matter of corporate philanthropy and charity, something praiseworthy and allowed, but not required.

Over the last decade, many corporations have established ethics programs and hired ethics officers who are charged with managing corporate ethics programs. Ethics officers do a great deal of good work, but it is fair to say that much of it focuses on compliance issues. The Sarbanes-Oxley Act created a dramatic and vast new layer of legal compliance issues. But is compliance with the law all that is required for behaving ethically? Though we will address this issue in greater detail in Chapter 5, let us briefly explore at this point several persuasive reasons for thinking that it is not sufficient in order to move forward to our discussion of ethics as perhaps a more effective guidepost for decision making.

First, holding that obedience to the law is sufficient to fulfill one’s ethical duties begs the question of whether or not the law itself is ethical. Dramatic examples from history, Nazi Germany and apartheid in South Africa being the most obvious, demonstrate that one’s ethical responsibility may run counter to the law. On a more practical level, this question can have significant implications in a global economy in which businesses operate in countries with legal systems different from those of their home country. Some countries make child labor or sexual discrimination legal, but businesses that choose to adopt such practices do not escape ethical responsibility for doing so. From the perspective of ethics, you do not forgo your ethical responsibilities by a blind obedience to the law.

Second, societies that value individual freedom will be reluctant to legally require more than just an ethical minimum. Such liberal societies will seek legally
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Realism Check: Ethics: Essential to Governance?

In 2003, Deloitte polled 5,000 directors of the top 4,000 publicly traded companies and reported that 98 percent believed that an ethics and compliance program was an essential part of corporate governance. Over 80 percent had developed formal codes of ethics beyond those required by Sarbanes-Oxley, and over 90 percent included statements concerning the company's obligations to employees, shareholders, suppliers, customers, and the community at large in their corporate code of ethics. Ethics clearly has gone mainstream. Further, corporate leaders have come to recognize that their responsibilities are much wider than previously thought. In practice, if not yet in theory, corporate America has adopted the stakeholder model of corporate social responsibility. Contemporary business now takes seriously its ethical responsibilities to a variety of stakeholders other than its shareholders.

| Have developed formal codes of ethics beyond those required by Sarbanes-Oxley | 83% |
| Have included statements concerning the company's obligations to stakeholders in code of ethics | 91% |


The law can be an efficient mechanism to prohibit the most serious ethical harms, but they will not legally require acts of charity, common decency, and personal integrity that may otherwise comprise the social fabric of a developed culture. The law can be an efficient mechanism to prevent serious harms, but it is not very effective at promoting goods. Even if it were, the cost in human freedom of legally requiring such things as personal integrity would be too high. Imagine a society that legally required parents to love their children, or even a law prohibiting lying.

Third, on a more practical level, telling business that its ethical responsibilities end with obedience to the law is just inviting more and more legal regulation. Consider the difficulty of trying to create laws to cover each and every possible business challenge; the task would require such specificity that the number of regulated areas would become unmanageable. Additionally, it was the failure of personal ethics among such companies as Enron and WorldCom, after all, that led to the creation of the Sarbanes-Oxley Act and many other legal reforms. If business restricts its ethical responsibilities to obedience to the law, it should not
be surprised to find a new wave of government regulations that require what were formerly voluntary actions.

Fourth, the law cannot possibly anticipate every new dilemma businesses might face, so often there may not be a regulation for the particular dilemma confronting a business leader. For example, when workplace e-mail was in its infancy, laws regarding who actually owned the e-mail transmissions, the employee or the employer, were not yet in place. As a result, one had no choice but to rely on the ethical decision-making processes of those in power to respect the appropriate boundaries of employee privacy while also adequately managing the workplace (see Chapter 7 for a more complete discussion of the legal implications of workplace monitoring). When new quandaries arise, one must be able to rely on ethics since the law might not yet—or might never—provide a solution.

Finally, the perspective that compliance is enough relies on a misleading understanding of law. To say that all a business needs to do is obey the law suggests that laws are clear-cut, unambiguous rules that can be easily applied. This rule model of law is very common, but not very accurate. If the law was clear and unambiguous, there wouldn’t be much of a role for lawyers and courts.

Consider one law that has significant impact of business decision making: the Americans with Disabilities Act. This law requires employers to make reasonable accommodations for employees with disabilities. But what counts as a disability and what counts as a reasonable accommodation? Over the years, claims have been made that relevant disabilities include obesity, depression, dyslexia, arthritis, hearing loss, high blood pressure, facial scars, and the fear of heights. Whether or not such conditions are covered under the law will depend on a number of factors, including how severe the illness is and how it affects the employee’s ability to work. Imagine that you are a corporate human resource manager and an employee asks that you make reasonable accommodations for her allergy. How would you decide if allergies and hay fever are disabilities under the Americans with Disabilities Act?

The legal answer is ambiguous. The law offers general rules that get specified in case law. Most of the laws that concern business are based on past cases that establish legal precedents. Each precedent applies general rules to the specific circumstances of an individual case. In most business situations, asking “Is this legal?” is really to ask “Are these circumstances similar enough to past cases that the conclusions reached in those cases will also apply here?” Since there will always be some differences between cases, this will always remain an open question. Thus, there is no unambiguous answer to the conscientious business manager who wishes only to obey the law. One simply cannot find the applicable rule, apply it to the situation, and deduce a decision from it.

It is worth remembering that many of the people involved in the wave of recent corporate scandals were lawyers. In the Enron case, for example, corporate attorneys and accountants were encouraged to “push the envelope” of what was legal. Especially in civil law where much of the law is established by past precedent, there is always room for ambiguity in applying the law. Further, in civil law there is a real sense in which one has not done anything illegal unless and until a court
decides that one has. This means that if no one files a lawsuit to challenge an action, it is legal.

As some theories of corporate social responsibility suggest, if a corporate manager is told that she has a responsibility to maximize profits within the law, a competent manager will go to her corporate attorneys and tax accountants to ask what the law allows. A responsible attorney or accountant will advise how far she can reasonably go before she would do something obviously illegal. In this situation, it would seem a manager has a responsibility to “push the envelope” of legality in pursuit of profits.

Most of the cases of corporate scandal mentioned at the start of this chapter involved attorneys and accountants who advised their clients that what they were doing could be defended in court. The off-book partnerships that were at the heart of the collapse of Enron and Arthur Andersen were designed with the advice of attorneys who thought that, if challenged, they had at least a reasonable chance of winning in court. At this point, the decision to “push the envelope” becomes more a matter of risk assessment and cost-benefit analysis than a matter of ethics. On this model, there is a strong incentive to assess the likelihood of being challenged in court, the likelihood of losing the case, the likelihood of settling for financial damages, and a comparison of those costs against the financial benefits of taking the action.

Because the law is ambiguous, because in many cases it simply is not clear what the law requires, business managers will often face decisions that will rely on their ethical judgments. To suggest otherwise is simply to hold a false picture of corporate reality. Thus, the fundamental ethical questions will confront even the businessperson who is committed to obeying the law. What should I do? How should I live?

As suggested previously, whether we step back and explicitly ask these questions or not, each one of us implicitly answers these questions every time we make a decision about how to act. Responsible decision making requires that we do step back to reflect upon and consciously choose the values by which we make decisions. No doubt, this is a daunting task. Fortunately, we are not alone in meeting this challenge. The history of ethics is the history of how some of the most insightful human beings have sought to answer these questions. Before turning to the range of ethical challenges awaiting each of us in the world of business, we will review some of the major traditions in ethics. Chapter 3 provides an introductory survey of several major ethical traditions that have much to offer in business settings.

**Ethics as Practical Reason**

In a previous section, ethics was described as practical and normative, having to do with our actions, choices, decisions and reasoning about how we should act. In light of this, we will describe ethics as a part of practical reason, reasoning about what we should do, and distinguish it from theoretical reason, which is reasoning about what we should believe. This book’s perspective on ethical decision making is squarely within this understanding of ethics as a part of practical reason.
Theoretical reason is the pursuit of truth, which is the highest standard for what we should believe. According to this tradition, science is the great arbiter of truth. Science provides the methods and procedures for determining what is true. Thus, the scientific method can be thought of as the answer to the fundamental questions of theoretical reason: What should we believe? So the question arises, is there a comparable methodology or procedure for deciding what we should do and how we should act?

The simple answer is that there is no single methodology that can in every situation provide one clear and unequivocal answer to that question. But there are guidelines that can provide direction and criteria for decisions that are more or less reasonable and responsible. We suggest that the traditions and theories of philosophical ethics can be thought of in just this way. Over thousands of years of thinking about the fundamental questions of how human beings should live, philosophers have developed and refined a variety of approaches to these ethical questions. These traditions, or what are often referred to as ethical theories, explain and defend various norms, standards, values, and principles that contribute to responsible ethical decision making. Ethical theories are patterns of thinking, or methodologies, to help us decide what to do.

The following chapter will introduce a model for making ethically responsible decisions. This can be considered as a model of practical reasoning in the sense that, if you walk through these steps in making a decision about what to do, you would certainly be making a reasonable decision. In addition, the ethical traditions and theories that we describe in Chapter 3 will help flesh out and elaborate upon this decision procedure. Other approaches are possible, and this approach will not guarantee one single and absolute answer to every decision. But this is a helpful beginning in the development of responsible, reasonable, and ethical decision making.

Opening Decision Point Revisited

Loyalty after a Crisis: Should Aaron Feuerstein Rebuild in Malden and Pay His Employees in the Meantime?

Malden Mills has been a favorite case of business ethics courses for many years. On the surface it provides a clear, if extreme, example of a business leader who was willing to make significant financial sacrifices for the well-being of his employees and community. Aaron Feuerstein could have made many other decisions that would have been financially beneficial, although at a great costs to employees and the surrounding towns. To many people, he was a true hero.

Yet, the case eventually became more complex. One important fact is that Malden Mills was privately owned. Had Feuerstein been CEO of a publicly traded corporation, his responsibilities would have been significantly different. Because of this fact, some observers describe Feuerstein’s decisions as a simple case of personal generosity, but not a helpful model for other corporate executives. As it was, Malden Mills was unable to recover financially from the losses associated with both the fire and Feuerstein’s decisions and eventually entered bankruptcy. Critics claim that this fact demonstrates the real costs of such generosity.
1. Other than ethical values, what values might a business manager use in reaching decisions? Are there classes in your college curriculum, other than ethics, which advise you about proper and correct ways to act and decide?

2. Why might legal rules be insufficient for fulfilling one’s ethical responsibilities? Can you think of cases in which a business person has done something legally right, but ethically wrong? What about the opposite—are there situations in which a business person might have acted in a way that was legally wrong but ethically right?

3. What might be some benefits and costs of acting unethically in business? Distinguish between benefits and harms to the individual and benefits and harms to the firm.

4. Review the distinction between personal morality and matters of social ethics. Can you think of cases in which some decisions would be valuable as a matter of social policy, but bad as a matter of personal ethics? Something good as a matter of personal ethics and bad as a matter of social policy?

5. As described in this chapter, the Americans with Disabilities Act requires firms to make reasonable accommodations for employees with disabilities. Consider such conditions as obesity, depression, dyslexia, arthritis, hearing loss, high blood pressure, facial scars, and the fear of heights. Imagine that you are a business manager and an employee comes to you asking that accommodations be made for these conditions. Under what circumstances might these conditions be serious enough impairments to deserve legal protection under the ADA? What factors would you consider in answering this question? After making these decisions, reflect on whether your decision was more a legal or ethical decision.

6. Do an Internet search on Malden Mills and research the present status of the business and Aaron Feuerstein’s ownership. How much of a difference would it make if Malden Mills was a publicly traded corporation rather than privately owned? Can any lessons be drawn from the present situation?

7. Construct a list of all the people who were adversely affected by the collapse of Enron. Who, among these people, would you say had their rights violated? What responsibilities, if any, did the managers of Enron have to each of these constituencies?

8. What difference, if any, exists between ethical reasons and reasons of self-interest? If a business performs a socially beneficial act in order to receive good publicity, or if it creates an ethical culture as a business strategy, has the business acted in a less than ethically praiseworthy way?

Key Terms

After reading this chapter, you should have a clear understanding of the following Key Terms. The page numbers refer to the point at which they were discussed in the chapter. For a more complete definition, please see the Glossary.

descriptive ethics, p. 8
ethical values, p. 12
ethics, p. 7
morality, p. 10

normative ethics, p. 8
norms, p. 11
practical reasoning, p. 16
stakeholders, p. 5

social ethics, p. 10
theoretical reasoning, p. 16
values, p. 12

Endnotes

Business has changed dramatically in the past few decades. Advances in technology, increasing globalization, heightened competition, shifting demographics—these have all been documented and written about extensively. Far less notice has been given to another, more subtle, change—one that is just as remarkable as these more visible developments. What I have in mind is the attention being paid to values in many companies today.

When I began doing research and teaching about business ethics in the early 1980s, skepticism about this subject was pervasive. Many people, in business and in academia, saw it as either trivial or altogether irrelevant. Some saw it as a joke. A few were even hostile. The whole enterprise, said critics, was misguided and based on a naïve view of the business world. Indeed, many had learned in their college economics courses that the market is amoral. Back then, accepted wisdom held that “business ethics” was a contradiction in terms. People joked that an MBA course on this topic would be the shortest course in the curriculum. At that time, bookstores offered up volumes with titles like The Complete Book of Wall Street Ethics consisting entirely of blank pages. The most generous view was that business ethics had something to do with corporate philanthropy, a topic that might interest executives after their companies became financially successful. But even then, it was only a frill—an indulgence for the wealthy or eccentric.

Today, attitudes are different. Though far from universally embraced—witness the scandals of 2001 and 2002—ethics is increasingly viewed as an important corporate concern. What is our purpose? What do we believe in? What principles should guide our behavior? What do we owe one another and the people we deal with—our employees, our customers, our investors, our communities? Such classic questions of ethics are being taken seriously in many companies around the world, and not just by older executives in large, established firms. Managers of recently privatized firms in transitional economies, and even some far-sighted high-technology entrepreneurs, are also asking these questions.

Ethics, or what has sometimes been called “moral science,” has been defined in many ways—“the science of values,” “the study of norms,” “the science of right conduct,” “the science of obligation,” “the general inquiry into what is good.” In all these guises, the subject matter of ethics has made its way onto management’s agenda. In fact, a succession of definitions have come to the forefront as a narrow focus on norms of right and wrong has evolved into a much broader interest in organizational values and culture. Increasingly, we hear that values, far from being irrelevant, are a critical success factor in today’s business world.

The growing interest in values has manifested itself in a variety of ways. In recent years, many managers have launched ethics programs, values initiatives, and cultural change programs in their companies. Some have created corporate ethics offices or board-level ethics committees. Some have set up special task forces to address issues such as conflicts...
of interest, corruption, or electronic data privacy. Others have introduced educational programs to heighten ethical awareness and help employees integrate ethical considerations into their decision processes. Many have devoted time to defining or revising their company’s business principles, corporate values, or codes of conduct. Still others have carried out systematic surveys to profile their company’s values and chart their evolution over time.

A survey of U.S. employees conducted in late 1999 and early 2000 found that ethics guidelines and training were widespread. About 79 percent of the respondents said their company had a set of written ethics guidelines, and 55 percent said their company offered some type of ethics training, up from 33 percent in 1994. Among those employed by organizations with more than 500 members, the proportion was 68 percent.

Another study—this one of 124 companies in 22 countries—found that corporate boards were becoming more active in setting their companies’ ethical standards. More than three-quarters (78 percent) were involved in 1999, compared to 41 percent in 1991 and 21 percent in 1987. Yet another study found that more than 80 percent of the Forbes 500 companies that had adopted values statements, codes of conduct, or corporate credos had created or revised these documents in the 1990s.

During this period, membership in the Ethics Officer Association, the professional organization of corporate ethics officers, grew dramatically. At the beginning of 2002, this group had 780 members, up from 12 at its founding 10 years earlier. In 2002, the association’s roster included ethics officers from more than half the Fortune 100.

More companies have also undertaken efforts to strengthen their reputations or become more responsive to the needs and interests of their various constituencies. The list of initiatives seems endless. Among the most prominent have been initiatives on diversity, quality, customer service, health and safety, the environment, legal compliance, professionalism, corporate culture, stakeholder engagement, reputation management, corporate identity, cross-cultural management, work–family balance, sexual harassment, privacy, spirituality, corporate citizenship, cause-related marketing, supplier conduct, community involvement, and human rights. A few companies have even begun to track and report publicly on their performance in some of these areas. For a sampling of these initiatives, see Figure 1.1.

To aid in these efforts, many companies have turned to consultants and advisors, whose numbers have increased accordingly. A few years ago, BusinessWeek reported that ethics consulting had become a billion-dollar business. Though perhaps somewhat exaggerated, the estimate covered only a few segments of the industry, mainly misconduct prevention and investigation, and did not include corporate culture and values consulting or consulting focused in areas such as diversity, the environment, or reputation management. Nor did it include the public relations and crisis management consultants who are increasingly called on to help companies handle values-revealing crises and controversies such as product recalls, scandals, labor disputes, and environmental disasters. Thirty or 40 years ago, such consultants were a rare breed, and many of these consulting areas did not exist at all. Today, dozens of firms—perhaps hundreds, if we count law firms and the numerous consultants specializing in specific issue areas—offer companies expertise in handling these matters. Guidance from nonprofits is also widely available.

What’s Going On?

A thoughtful observer might well ask “What’s going on?” Why the upsurge of interest in ethics and values? Why have companies become more attentive to their stakeholders and more concerned about the norms that guide their own behavior? In the course of my teaching, research, and consulting over the past two decades, I have interacted with executives
and managers from many parts of the world. In discussing these questions with them, I have learned that their motivating concerns are varied:

An Argentine executive sees ethics as integral to transforming his company into a “world-class organization.”

A group of Thai executives wants to protect their company’s reputation for integrity and social responsibility from erosion in the face of intensified competition.
A U.S. executive believes that high ethical standards are correlated with better financial performance.

An Indian software company executive sees his company’s ethical stance as important for building customer trust and also for attracting and retaining the best employees and software professionals.

A Chinese executive believes that establishing the right value system and serving society are key components in building a global brand.

The executives of a U.S. company see their efforts as essential to building a decentralized organization and entrepreneurial culture around the world.

Two Nigerian entrepreneurs want their company to become a “role model” for Nigerian society.

A Swiss executive believes the market will increasingly demand “social compatibility.”

An Italian executive wants to make sure his company stays clear of the scandals that have embroiled others.

A U.S. executive believes that a focus on ethics and values is necessary to allow his company to decentralize responsibility while pursuing aggressive financial goals.

A U.S. executive answers succinctly and pragmatically, “60 Minutes.”

These responses suggest that the turn to values is not a simple phenomenon. Individual executives have their own particular reasons for tackling this difficult and sprawling subject. Even within a single company, the reasons often differ and tend to change over time. A company may launch an ethics initiative in the aftermath of a scandal for purposes of damage control or as part of a legal settlement. Later on, when the initiative is no longer necessary for these reasons, a new rationale may emerge.

This was the pattern at defense contractor Martin Marietta (now Lockheed Martin), which in the mid-1980s became one of the first U.S. companies to establish what would later come to be called an “ethics program.” At the time, the entire defense industry was facing harsh criticism for practices collectively referred to as “fraud, waste, and abuse,” and Congress was considering new legislation to curb these excesses. The immediate catalyst for Martin Marietta’s program, however, was the threat of being barred from government contracting because of improper billing practices in one of its subsidiaries.

According to Tom Young, the company president in 1992, the ethics program began as damage control. “When we went into this program,” he explained, “we didn’t anticipate the changes it would bring about. . . . Back then, people would have said, ‘Do you really need an ethics program to be ethical?’ Ethics was something personal, and you either had it or you didn’t. Now that’s all changed. People recognize the value.” By 1992, the ethics effort was no longer legally required, but the program was continued nonetheless. However, by then it had ceased to be a damage control measure and was justified in terms of its business benefits: problem avoidance, cost containment, improved constituency relationships, enhanced work life, and increased competitiveness.

A similar evolution in thinking is reported by Chumpol NaLamlieng, CEO of Thailand’s Siam Cement Group. Although Siam Cement’s emphasis on ethics originated in a business philosophy rather than as a program of damage control, Chumpol recalls the feeling he had as an MBA student—that “ethics was something to avoid lawsuits and trouble with the public, not something you considered a way of business and self-conduct.” Today, he says, “We understand corporate culture and environment and see that good ethics leads to a better company.”
Siam Cement, one of the first Thai companies to publish a code of conduct, put its core values into writing in 1987 so they “would be more than just words in the air,” as one executive explains. In 1994, shortly after the company was named Asia’s “most ethical” in a survey conducted by *Asian Business* magazine, Chumpol called for a thorough review of the published code. The newly appointed CEO wanted to make sure that the document remained an accurate statement of the company’s philosophy and also to better understand whether the espoused values were a help or hindrance in the more competitive environment of the 1990s. In 1995, the company reissued the code in a more elaborate form but with its core principles intact. The review had revealed that while adhering to the code did in some cases put the company at a competitive disadvantage, it was on balance a plus. For example, it helped attract strong partners and employees and also positioned the company, whose largest shareholder was the Thai monarchy’s investment arm, as a leader in the country.

A very different evolution in thinking is reported by Azim Premji, chairman of Wipro Ltd., one of India’s leading exporters of software services and, at the height of the software boom in 2000, the country’s largest company in terms of market capitalization. Wipro’s reputation for high ethical standards reflects a legacy that began with Premji’s father, M.H. Hasham Premji, who founded the company in 1945 to make vegetable oil. The elder Premji’s value system was based on little more than personal conviction—his sense of the right way to do things. Certainly it did not come from a careful calculation of business costs and benefits. In fact, his son noted, “It made no commercial sense at the time.”

When his father died in 1966, Azim Premji left Stanford University where he was an undergraduate to assume responsibility for the then-family-owned enterprise. As he sought to expand into new lines of business, Premji found himself repeatedly having to explain why the company was so insistent on honesty when it was patently contrary to financial interest. Over time, however, he began to realize that the core values emphasized by his father actually made for good business policy. They imposed a useful discipline on the company’s activities while also helping it attract quality employees, minimize transaction costs, and build a good reputation in the marketplace. In 1998, as part of an effort to position Wipro as a leading supplier of software services to global corporations, the company undertook an intensive self-examination and market research exercise. The result was a reaffirmation and rearticulation of the core values and an effort to link them more closely with the company’s identity in the marketplace.

Managers’ reasons for turning to values often reflect their company’s stage of development. Executives of large, well-established companies typically talk about protecting their company’s reputation or its brand, whereas entrepreneurs are understandably more likely to talk about building a reputation or establishing a brand. For skeptics who wonder whether a struggling start-up can afford to worry about values, Scott Cook, the founder of software maker Intuit, has a compelling answer. In his view, seeding a company’s culture with the right values is “the most powerful thing you can do.” “Ultimately,” says Cook, “[the culture] will become more important to the success or failure of your company than you are. The culture you establish will guide and teach all your people in all their decisions.”

In addition to company size and developmental stage, societal factors have also played a role in some managers’ turn to values. For example, executives in the United States are more likely than those who operate principally in emerging markets to cite reasons related to the law or the media. This is not surprising, considering the strength of these two institutions in American society and their relative weakness in many emerging-markets countries. Since many ethical standards are upheld and reinforced through the legal system, the linkage between ethics and law is a natural one for U.S. executives. In other cases, executives...
offer reasons that mirror high-profile issues facing their industries or countries at a given
time—issues such as labor shortages, demographic change, corruption, environmental
problems, and unemployment. Antonio Mosquera, for example, launched a values initia-
tive at Merck Sharp & Dohme Argentina as part of a general improvement program he set
in motion after being named managing director in 1995. Mosquera emphasized, however,
that promoting corporate ethics was a particular priority for him because corruption was a
significant issue in the broader society.

Despite the many ways executives explain their interest in values, we can see in their
comments several recurring themes. Seen broadly, their rationales tend to cluster into four
main areas:

- Reasons relating to risk management
- Reasons relating to organizational functioning
- Reasons relating to market positioning
- Reasons relating to civic positioning

A fifth theme, somewhat less salient but nevertheless quite important for reasons we
will come back to later, has to do with the idea simply of “a better way.” For some, the
rationale lies not in some further benefit or consequence they are seeking to bring about but
rather in the inherent worth of the behavior they are trying to encourage. In other words, the
value of the behavior resides principally in the behavior itself. For these executives, it is just
better—full stop—for companies to be honest, trustworthy, innovative, fair, responsible,
or good citizens. No further explanation is necessary any more than further explanation is
required to justify the pursuit of self-interest or why more money is better than less.

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Reading 1-2

An Ethical Hero or a Failed Businessman?
The Malden Mills Case Revisited
Penelope Washbourne

Introduction

At the annual meeting of the Society for Business Ethics in Boston in 1997 the guest
speaker was Aaron Feuerstein, the acclaimed CEO of Malden Mills, who brought tears
to the eyes of skeptical academics with his tales of the mill fire in 1995 and his generous
actions towards his employees. I had written a case about him during the winter of 1996 and
suggested him as a guest speaker for the annual meeting. After the meeting, I was given a
guided tour of the gleaming rebuilt factory in Lawrence, Mass., and was duly impressed by
the state of the art manufacturing technology used to make that cozy fleece, Polartec, which
is made from recycled plastic. Aaron Feuerstein’s star continued to shine in the business
press, and even in 2004, as a hero who paid his employees for a number of months after the
fire destroyed their jobs.

As many noted then and now, here was a true man of virtue, an ethical giant in a busi-
ness world of massive layoffs such as those at AT&T and Sunbeam, and when compared
with colossal failures in leadership in many huge corporations.
I taught this case over the years, with video clips from the national media, in my business ethics courses and was subsequently told by students that the case had made a powerful impression on them. Maybe it was the pictures of those desperately anxious mill workers with their tears and gratitude responding to Feuerstein’s announcement after the fire that he was going to continue to pay his workers for another month. “You’re a saint” said one. Or maybe it was Feuerstein’s own tears that affected my students?

The case touched a deep nerve: here was a business man who put the care of his workers above the bottom line. My goal in writing and teaching about this case was to demonstrate that it is better to teach business ethics with examples of ethical leadership than to continue to focus on, as most of our case books do, the multiple failures in moral leadership in corporate life. Even formerly exemplary companies can fall under an ethical cloud.

Subsequently, though I read that Malden Mills had gone bankrupt, since the tenth year anniversary of the fire was in 2005, I decided to take another look at what the effect had been on the local community of Aaron Feuerstein’s actions after the fire. My reading of the events that have taken place since the fire raises an important dilemma for teaching this tale of ethical virtue. What has been the aftermath? It would be nice to say that the gleaming new mill saved the jobs in the community and that Aaron Feuerstein is still in charge of his grandfather’s firm, well loved by his workers and local politicians for preserving the one remaining industry in an area of high unemployment.

It would be nice to say that not only is virtue its own reward, but also that it is indeed rewarded by the world. For Aaron Feuerstein and his family firm, unfortunately this is not the case. The actual story is more complex than that, as is often the case in real life.

To describe it briefly: Aaron borrowed money to rebuild the mill, beyond the money he would finally receive from the insurance company. He built a large facility, counting on the expansion of his Polartec fleece lines and the continuation of his brand of upholstery fabrics. His debt was more than his final insurance settlement, the upholstery business proved a failure and he decided to get out of it, cheap competition and an unseasonably warm winter cut into his Polartec sales and he had to declare bankruptcy in 2001. The firm remained under bankruptcy protection until 2003, but Aaron lost control of the company and GE Capital, the main creditor with 16.6 percent, became its largest shareholder, with a dominant influence on the new board. In July 2004 the board hired a new executive. A new manufacturing operation has been opened in China. Jobs in Lawrence and nearby New Hampshire have declined. In the meantime, Aaron and his son Daniel with a group of investors and a commitment to keep jobs in the local communities, attempted to buy back the firm. Their offers were rejected.

How indeed will I teach this case now? Were Aaron’s actions after the fire virtuous or reckless? Did his hope for the future and his commitment to the local community blind him to the economic realities of the industry at the time and cause him to overbuild, and so put the whole company in jeopardy? From a utilitarian perspective, did he do the right thing? What was the long-term effect of his actions on the community?

I decided that I had to get close to the source and elected to spend a few days in Lawrence, Massachusetts, and I was able to interview Aaron Feuerstein in his home in Boston. When I interviewed Aaron in November 2004, he said he felt he had failed.

Lawrence, Massachusetts

In fall 2004, the main impression of Lawrence as a community to a visitor unfamiliar with depressed mill towns in New England was decay. The massive empty mill buildings along the Merrimack River have forlorn signs for “Space Available,” as if the next high-tech boom was going to transform this now virtual ghost town into a thriving business community.
Along the main street with its closed businesses, even the Goodwill center was shuttered. The one remaining open facility was a large Headstart center with its brightly colored plastic play structures. The impression was that this must be a city that is heavily funded with federal grant monies for low income families.

Though large trash receptacles ready for collection lined the narrow residential streets the day I was there, they did not contain the abandoned sofas and junk in the empty lots. The local community newspaper, printed in Spanish and English, spoke of the challenge of trash as a neighborhood problem. The mayor wanted to put awnings over the shops in the main streets, to attract business downtown. Among the nail salons and the few ethnic food establishments, one set of buildings, and one alone, remained a viable concern, Malden Mills Inc. Located next to the Arlington section of town, one of the poorest neighborhoods, the mill is the only sizable employer in Lawrence, Massachusetts.

Five hundred of its employees live in a five mile radius of the mill and many walk to work. It would be fair to say that the economic well-being of Lawrence and its nearby community in New Hampshire, pressured by the 2004 $2.50 an hour wage, is intimately connected to the well-being of the one remaining manufacturing facility paying union wages at an average rate in 2004 of $12.50 an hour, with benefits. The unemployment rate in Lawrence has remained at two and a half to three times the state average for the last 20 years, between 10 and 15 percent since 1983. The academic standings of the local schools are the lowest in the state.

My trip to Lawrence answered my question: Why did Aaron Feuerstein feel and still feel today such a fierce loyalty and sense of obligation to the community of Lawrence and its neighboring towns? What did it mean to those communities that he decided to rebuild the mill and commit to pay his employees for several months after the fire? As he told me, the tears of the workers after the fire were not tears of gratitude towards him, but recognition that without the mill there was nothing left for them, their future, or their community.

### The 72,000 People of Lawrence and Their History

This city calls itself the “city of immigrants.” It claims that 45 different nationalities and ethnicities have lived in Lawrence. It was founded as a mill town in 1842 to establish woolen and cotton mills and to exploit the new technology of water power along the swift-flowing rivers. The large labor pool required for the factories was imported, and consisted largely of women and immigrants, who lived in dormitories and boarding houses. At its peak, between 1890 and 1915, there were 90,000 residents in Lawrence.

Lawrence was the site of the famous “Bread and Roses” strike in 1912 when after nine weeks of a strike for better conditions during a harsh winter, the company bosses brought the state militia out to attempt to force the 30,000 strikers into submission and prevent them from shipping their children out to relatives and sympathetic families in other communities.

Thus, over the years, Lawrence became known for being in the forefront of the struggle for workers’ rights and for the right to organize unions. Now earlier generations of Scots and Irish and Eastern European immigrants have been replaced by Puerto Ricans and first-generation immigrants from Central America. Their mill jobs allow them the ability to function in their native languages, a rare option in high-paying employment where knowledge of English is often a necessity.

Though most of Lawrence’s jobs have disappeared as the mills finally closed after World War II, Aaron Feuerstein’s commitment to continuing his operation in this immigrant, unionized town is unique. It stems from a recognition of the value of his own family’s history and his grandfather’s legacy. As a Hungarian Jewish immigrant in New York City at the turn of the century, his grandfather sold dry goods and eventually moved to Massachusetts.
and began the family firm in 1907. Aaron remembers his roots and the history of earlier generations of immigrant labor who formed the economic engine that brought succeeding generations to a better way of life. His antipathy to shipping jobs South and to offshoring manufacturing jobs at the expense of domestic workers comes from a profound respect for the skills of those who worked hard to build a future for their families in this country.

Though Aaron had indeed laid off workers due to business conditions, nevertheless he believes we owe these workers in this community an opportunity to perform on the job, for themselves and the community. This is a relationship of mutual respect and obligation that has been carried through three generations of Feuersteins towards their union workers and their communities in Massachusetts and New Hampshire. Aaron spoke proudly of never having had a strike over the years and of having tough but fair negotiations with the unions during his tenure in the company.

Knowing of Aaron’s commitment to keep jobs in the local community, the union leadership had hoped that the Feuersteins would be successful in their efforts to regain control of the company. Since the advent of the new company management, the union threatened a strike last fall in November 2004, but finally settled on a new contract.

Aaron had resurrected himself once before when he went bankrupt in the 1980s. His technological innovations captured a new market in fleece material which he branded under the name of Polartec for garments for outdoor enthusiasts. His workers had come through for him in that difficult time. Once again he believed he could resurrect his company from the ashes. Could he do it again?

Aaron’s sense of failure, at this point in his life (he was 80 in 2005), paternalistic though it may sound, may have to do with failing to live up to the legacy of the family firm that had been handed to him, failing the very community he had pledged to support with good jobs, and failing to protect them from the cost-cutting strategies in which wages are just an expense.

**The Business Strategy and Hope for Lawrence**

When fleece was invented it filled a wonderful need in the market for garments that did not become wet with moisture and perspiration, as cotton did, but were wickable, allowing the person to stay warm. Aaron’s strategy was to pursue research and development and create high-end, high-quality products that could be recognized as a brand: “Polartec.” Since its first invention the number of different weights, colors, and features has exploded, with windproof features and even designs for children’s outerwear. Aaron believed that Malden Mills could stay ahead of increasing competition of offshore manufacturers and the “com-modification” of the industry by staying ahead of the innovation curve. Fleece was soon everywhere, not just in high-quality jackets for climbers and winter sports enthusiasts, but in regular articles of clothing for adults and children, as well as blankets and throws.

After the fire, even though one of his main customers, Lands’ End, initially showed support and featured the story of the mill’s fire and Aaron’s actions towards his employees in its spring 1996 catalogue, Aaron eventually lost major customers, including Lands’ End, which sought other suppliers. Along with the interruption in supply, apparently the Polartec brand did not have the power in the general market, except in specialized high-end products, to withstand the flood of cheaper goods coming from Asia.

After the fire another of his product lines, jacquard upholstery velvet, proved to be unsuccessful in earning a brand identity. Furniture manufacturers were unwilling to pay the premium for a branded fabric and in 1998, Aaron got out of that business. It represented about 50 percent of the company’s business at the time of the fire, and its production lines were hard hit by the fire and took longer to resume operation than the polarfleece lines.
One business strategy implemented after the fire by one of the company’s former executives, Cesar Aguilar, who spent an uncomfortable weekend in wet clothing as part of his military reserve training, is beginning to pay off for the company and for the community, however. Malden Mills is supplying warm winter clothing to the troops in Afghanistan and Iraq as well as conducting research into new lightweight electronic high-tech fabrics that soldiers can wear next to their skin and that can monitor their vital signs and be of assistance in determining injuries. Another innovation is a next-to-skin fabric that would prevent the growth of bacteria and odor for soldiers who are out in the field. The U.S. military approved $21 million for Polartec garments for 2005, a portion of which goes to the garment manufacturer. That figure includes $1.5 million for research.

The military contracts offer a ray of hope for the company. Not only must all products made for the U.S. Armed Services be made in the United States, but the innovations in new products designed for military use can be developed into commercial applications in the future. In addition, according to a company spokesman the military business is not seasonal, which makes it easier to balance the workload. The military contract currently represents about 20 percent of Malden Mills’ business.

What Went Wrong?

After a traumatic event such as the fire, one’s decision making capacity is impaired. I know this from personal experience, having escaped from the Oakland Hills fire in 1991 where almost 3,000 homes were destroyed and 24 people ultimately died. I think my interest in this case certainly was influenced by having had this common experience. After a fire, “post-traumatic distress” is an important factor. Aaron even witnessed his factory burning down. In the aftermath of the fire, the shock and sense of loss are enormous, and yet major decisions that have a long-term impact must be made immediately. Relations with family and friends are strained. In Aaron’s case, he had a huge sense of responsibility for the injured workers, several of whom were badly burned, though luckily none died, and for those who risked their lives to save parts of the buildings that were not so heavily engulfed. In addition, the fire happened just before Christmas. Though some members of his board, which included members of his own family who worked in the company, opposed it, Feuerstein generously offered to pay his idled workers for the following month, even though he was not required to do so. He said he did not do it for the publicity, but because he was firmly convinced it was the right thing to do. But in hindsight, was it the right thing to do?

Feuerstein renewed his pledge to his 1,500 employees for another three months. As the news spread of his actions he received about $1 million in donations, from small to large checks from all around the country. By the end of a month some of his operations were up and running again as they shifted equipment undamaged by the fire to other locations. Some of the manufacturing facilities for Polartec had been spared.

Was Feuerstein’s generosity to his employees a costly decision that ultimately put his company in jeopardy? It cost about $15 million. One view is that by itself it may not have been a foolhardy decision, given the growing business he was in. Sales of Polartec had been growing by 50 percent annually at the time of the fire. Aaron also knew that if his business was going to have a chance to rebuild, he was going to have to rely heavily on his workers to put in an extraordinary effort to get him up and running again.

After three months the remaining workers who were still out of work were supported by unemployment and special funds from the gifts that had been donated.

The outpouring of support, both financial and in the public arena, surprised Feuerstein. He was a private man, an owner of a small family firm, little known outside of New England,
and now all of a sudden he was in front of the cameras, making statements about the state of American business. He was invited to sit behind Hillary Clinton at President Clinton’s State of the Union Address in January 1996. The names of Malden Mills and Aaron Feuerstein were in all the press and created a flood of goodwill for the company.

He was lauded not only for paying his workers after the fire, but for his immediate commitment to rebuild the factory in the same location. As he said so frequently in interviews after the fire, he and his father had not moved the operation to the South as many other mills did in search of cheaper labor in the 1950s and 1960s, so why would he abandon Lawrence now? He continues to believe that highly skilled labor can produce the best quality products, which in turn can differentiate a company from its competition, and that there is still a place for manufacturing in this country. This commitment earned him enormous political support from the local politicians, the governor, Senators Kennedy and Kerry, and New Hampshire representatives.

The Decision to Rebuild

At issue seems to be not the fact of rebuilding in Lawrence, but the manner in which Aaron Feuerstein proceeded on this project.

Aaron knew that he was “fully insured.” What he did not know, what no claimant after a loss knows, is what the actual payout amount will be. He would not know that for many months of negotiations with the insurer. At the point of a claim, the relationship with the insurer turns from one of being, as it were, “in good hands” to one that is adversarial in nature.

The insurer tries to keep the settlement as low as possible and the claimant wants to replace the buildings that burned. The insurer AGI was a tough negotiator, settling well after the newly rebuilt factory had been completed in 1997. The final insurance settlement was about $300 million, covering only 75 percent of the $400 million in rebuilding costs that Feuerstein had borrowed to put his factory in operation.

Was Aaron’s decision to rebuild in the immediate aftermath of the fire one of an emotion-driven “survival instinct”? The firm’s famous clock tower had been saved during the fire. How could Aaron not see that as a symbol of the firm’s commitment to rise from the ashes? Was the idea of renting or renovating facilities, or scaling down the size, never seriously considered? Was the promise of all that cash that would allow him to replace aging equipment with brand new machines, to build a new state of the art facility to deal with the overbearing heat in summer and accommodate the new computerized methodologies, a license to spend more than he should?

Even within the context of rebuilding it was clear that Aaron thought big and wanted the best. There was dispute among the members of the board and with his own son about the scale of the rebuilding. The insurance coverage did not specify that the buildings had to be rebuilt at all or require a minimal square footage, but Aaron opted for the best. He replaced almost all of the space that had been lost, anticipating that his Polartec sales would continue to grow, even though his son was advising him to scale back the square footage. He later admitted that maybe his building plans had been overly extravagant, even to the point of buying new equipment, whereas before the fire he would have bought used. While the mill was being rebuilt, he had leased space for some of his operations in neighboring towns, but now it was he who was to have excess space as the business turned down.

What was Aaron’s failure? Did he fail to anticipate the great gap between his rebuilding costs and his final insurance settlement? Did he fail to anticipate that in spite of great attention and support on one level from all the media, months of interruption of his supply would enable his competitors to gain an edge and win customers? Was his attention so
focused on recovery from the fire and its aftermath, the insurance claims, and the lawsuits against the company from injured employees, that he failed to see the business risks? Was he imprudent or unlucky that a warm winter depressed fleece sales just at the time his upholstery line was floundering? Was Aaron Feuerstein trying to singlehandedly buck the inexorable pressure on the costs of manufacturing and prices that eventually led the new board after the bankruptcy to a partnership with a mill in China? In 2004 this outsourced production was at about 10 percent of production, but that figure is likely to rise due to the expiration of the textile tariffs with China in January 2005.

The Legacy

Under the special arrangements of the bankruptcy settlement, Aaron and his sons had an opportunity to bid on the firm for another year, but their bids were rejected by the current owners. His group of financial investors, along with the Import-Export Bank, which had guaranteed a loan, had plans to develop the excess mill space into mixed income housing units and retain jobs in the local area. Though Aaron at 79 had surgery on his heart in July 2004, his determination to regain control over the company remained undimmed. He feared it would become another commodity company and the original vision of investing in innovative products that require a highly skilled workforce would be lost. He did not want to run the mill as CEO, but he wanted to resurrect the legacy of the family firm, committed to the goal of continuing to provide high-quality, well-paying jobs to the people of Massachusetts and New Hampshire.

If it were dependent solely on the force of his personality, it would have happened. Aaron is an obstinate man. The local politicians were supporting him, hoping that he could be given the chance to preserve the jobs in the local area.

Since Aaron failed to regain control of the family firm, has he failed? He believes that he has. But as a former journalist at the Boston Globe assures him, “You have won, Aaron, no matter what happens!” His ethical legacy is independent of whether or not his family regains control of Malden Mills.

Though his enterprise may have failed, he rebuilt the mill in Lawrence and gave the community hope that there is a future for their families. The new owners currently repeat their commitment to the community, though they state that more jobs will probably be offshored in the future.

What Aaron did was indeed an example of virtue ethics since it was in his character to be concerned for his employees. Examples of his prior support for them, such as giving assistance to help buy a house or send a child to college, were recounted by workers after the fire. However, what Aaron did in paying his workers after the fire was more a demonstration of Carol Gilligan’s “Ethic of Care,” shaped by the importance of preserving relationships. When faced with the decision of what he could do for his workers he asked himself the question, not what was his duty to do, but what was the most loving thing to do?

This act has called American business leaders to consider again the employment relationship between an enterprise and its workers, not as being exclusively an economic one, but also a personal and communal one. Aaron Feuerstein’s acts, which put his workers’ needs above his own economic self-interest, were grounded in his religious convictions as an orthodox Jew. He believes he has a responsibility to them as individuals and to the common good. He had the unique chance to show that rather than pursuing the course of the moral minimum, he chose the moral maximum. As he said to me, “At the end of the day, at the Final Judgment, will it be enough to say, ‘I have been the CEO of a company and made a lot of money? ’ After your basic needs are met, what is the point of all that activity, if not to do some good? … on Judgment Day what do you amount to?”
In the retail outlet at Malden Mills among the colorful bolts of cloth and remnants are two images that caught my attention. One was a portrait of Aaron Feuerstein made out of different colored cotton spools, a diffuse image made by an employee.

The other was a wall hanging embroidered by children at a synagogue school as a gift in thanks to Aaron for his support of them. What is his legacy? He is clearly loved.

Aaron is a unique businessman: He lives modestly and his heavily thumbed Bible sits on his table beside his two volumes of Shakespeare’s comedies and tragedies.

He reads them frequently.

Is this a tragic tale? Maybe, but for Shakespeare’s best tragic heroes, their defeat at the hands of fate is not the end. The truth of their life lives on.

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Reading 1-3

Do You Need an Ethics Officer?

Jon Entine

“We Have Seen the Enemy and He May Be Us”

Frank Daly has steered an unusual career path. A devout Catholic, the Boston native went to seminary before going to Rome to study at the Gregorian University. He became a priest and for eight years served as an assistant pastor. For a time, he was a university chaplain. He dedicated his life to living in God’s reflection.

So how did Frank Daly end up as a corporate director at Northrop Grumman, the southern California–based defense contractor? Daly is an “ethics officer,” one of a new generation of corporate managers who believe that “business ethics” need not be an oxymoron.

An ethics officer? After all, isn’t business war? Or as professor Theodore Levitt once wrote in the Harvard Business Review, “Business must fight as if it were at war. And, like a good war, it should be fought gallantly, daringly, and above all not morally.”

Times have changed. The renewed focus on corporate ethics has come about as a response to the public outcry and avalanche of lawsuits that accompanied the business scandals of the anything-goes go-go ’80s: Dennis Levine, Ivan Boesky, Charles Keating, Michael Milken, international bribery. The movement to hire ethical officers gathered steam with the extension of the Federal Sentencing Guidelines to executives in 1991—they now face the prospect of jail time as a result of wrongdoing by subordinates.

Companies have learned that ethical programs can avoid expensive litigation and keep skeletons off the front page of The Wall Street Journal—which pays off handsomely in company loyalty and burnishes a corporation’s reputation. That goes right to the bottom line.

In response to embarrassing disclosures such as toilet seats and hammers costing hundreds of dollars, and with the design in part to ward off more government oversight, military contractors launched an initiative in the ’80s to bolster legal and ethical compliance. The southern California region is peppered with defense-related companies that have full-time ethics officers: Northrop Grumman, which has a plant in Oxnard; Whittaker in Simin Valley; Lockheed Martin, whose companywide ethics office is in Westlake Village; and Litton in Woodland Hills. The former head of the defense industry initiative was recently hired by Columbia HCA, which runs Las Robles Hospital, to clean up its scandal-tinged operation. Other area companies with ethics officers include Southern California Edison, Avery Dennison, and Earthlink.
“The goal of an ethics officer, my goal, is not only to insure that we are operating in legal compliance but that we bring a strong, personal sense of values to our everyday experience in the workplace,” says Daly. “Corporations are publicly owned, after all. They no longer act—they no longer should act—as if they have no accountability. I think we’re making some real progress.”

To many, this rings of public relations fluffery. But Daly is anything but a spin artist. After leaving the priesthood, he went to work in Massachusetts politics, first in the Dukakis administration and then as an aid to Paul Tsongas. The ethics initiatives at Northrop caught Daly’s attention. He signed on as division manager of communications and public relations and was promoted to director of ethics and business conduct. Shortly thereafter, a crisis rocked the company, prompting an agonizing appraisal of its corporate culture.

Back in 1987, Northrop’s Pomona, California, operation was making flight data transmitters for cruise missiles and sensors to stabilize the AV-8B Harrier Jump Jet. Northrop’s tests indicated that the parts functioned perfectly. But in the real world, both parts failed miserably. Operating on an anonymous tip, the FBI raided the plant, eventually charging 11 individuals and Northrop itself with 189 counts of fraud and conspiracy.

What had gone wrong?

It turns out that Pomona engineers had long recognized that the equipment used to test the missile components occasionally malfunctioned. When this happened, they substituted a printout from a prior successful test. As for the Harrier Jump Jet, the chief engineer would later confess that they had falsified vibration-level tests. Pomona managers said they felt pressure to find a way to pass the units even without adequate testing equipment. They had convinced themselves that their futures and millions of company dollars were on the line.

Ironically, and unfortunately for them, they were right. The Pomona plant was subsequently shuttered, most of the managers fired, and in 1989, Northrop paid a $17 million fine.

President Kent Kresa was apoplectic. “This isn’t the case of a few rotten apples,” he fumed. It was a corrupted corporate culture. “I think we have to blame our own process,” he said. “It could be a problem in the future if we don’t stamp it out.” Northrop employees at division headquarters in suburban Boston joined in the outrage at the betrayal in Pomona.

“We found errors principally of management,” Air Force investigators agreed. “Not so much of employees not being concerned about ethical conduct but the failure of the management system to open these up, bring them to light.”

Part crisis manager, part corporate theologian, Daly was called upon to do nothing less than to address employee doubts about the internal ethics of the company and institute constructive, long-term solutions. He wasn’t looking for legal Band-Aids but to overhaul the corporate culture and introduce higher standards of accountability. The challenge tapped into Daly’s lifelong passion for personal responsibility.

“We aren’t in the business of teaching people how to be ethical,” said Daly. “We’re teaching ethical people how to make a good decision when it could be difficult.”

It’s easy for people to say they would not cut corners when presented with the choice faced by the engineers in Pomona. But as with most real-life dilemmas, the pressures can be overwhelming to those in the ethical crucible. They feared for their jobs and had convinced themselves that no one would be the wiser for their short-cuts. In fact, they had no place to turn—there were no clear companywide ethical standards, no ethical hotline, and no ombudsmen to take their concerns to.

Daly helped draw up a code of ethics that was both inspirational and practical—not just bromides about “doing the right thing.” With the backing of Kresa, who navigated the crisis and was later named CEO of the merged Northrop Grumman, Daly oversaw the “Northrop
Leadership Inventory,” which attempts to evaluate the linkage of behavior, values, and leadership conflict resolution. To help employees make tough ethical calls, the company distributes guidelines that it calls “When to Challenge” and “When to Support.” Employees also can call an ethics hotline, which is both confidential and responsive. Some 30 percent of the calls allege actual wrongdoing, about half of which check out. “Mostly, the hotline offers an outlet for employees to diffuse potential crises before they lead to unethical or unlawful behavior,” Daly says.

At many corporations, crisis management, ethics, and brand management are now closely intertwined. Twenty years ago, says Daly, many businesses did not believe they had a duty beyond the minimum dictates of the law. “That just doesn’t work today,” he says. “A small number of wayward employees can sink an organization. We’ve learned that the hard way at Northrop Grumman. For companies to survive, they have to learn to be pro-active in the gray areas of business. That’s where the tough decisions are made. That’s when ethics pays off.”

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