## Chapter 10

**ETHICS AND**

**SOCIAL RESPONISBILITY OF BUSINESS**

## 

*How much of the manufacturing waste* should *we dump in the water?*

**I. Overview**

The novel *Spartacus* was written by the French author Bernard Joseph Saurin in 1760. The novel was named after the Thracian slave who died in 71 B.C. after leading a revolt against the Roman authorities. In this novel, Saurin wrote: "The law often permits what honor forbids." That quote truly encapsulates what the study of ethics vis-à-vis law is all about. While it may have been legal to trade in human misery and subjugation, could it ever be morally acceptable under any of the systems of ethics discussed in this chapter?

The study of ethics revolves around the examination of rules, conduct, and character through a morally-tinted microscope. That law should be grounded in some sort of morality-based foundation is self-evident. Yet painful history has shown us over and over the prices paid when there is an abyss between law and ethics. Sometimes these gaps can only be closed by conflagrations and wars so costly that we are reminded of an old anonymous proverb: "Adam ate the apple, and our teeth still ache."

The goals of all the ethical schools of thought are to seek some sort of morally-based rationale for human behavior. This rationale may be found in outside sources as seen in schools of ethical fundamentalism or in the rule that provides the greatest good to society as illustrated by utilitarianism. Others such as Kant and Rawls have sought to devise formulas of behavior based on universal rules or social contract, respectively. In all these systems, a morally-based methodology is sought as a guidepost for behavior. If these guideposts are universally accepted, the odds are very high that they will no longer be advisory, but rather required by law. The process by which morally-based ethical behavior is first desired, then expected, and finally mandated is really the evolution of law. Note that law is the last stage in this often painful process.

Because so much of our legal and economic activities are conducted in the corporate format, juristic (law-made) business entities cannot ignore this constant and dynamic tug and pull between ethics and law. We have either come a long way or become hopelessly bogged down in political correctness depending on your personal point of view. This dynamic is well illustrated by the differences between the thinking of the court in *Dodge v. Ford Motor Company* in 1919 and today's social audits of corporate citizenship. The bottom line in the study of ethics is ultimately personal. Imagine a world without a concern for law and ethics. As French author Stephanie Félicité Genlis said in 1793, “The man whose probity consists in merely obeying laws cannot be truly virtuous or estimable; for he will find many opportunities of doing contemptible and even dishonest acts, which laws cannot punish.”

**II. Hypothetical Multi-Issue Essay Question**

Taxes are a cost of not only doing business but also an expense of living in a free society. As Justice Oliver Wendell Holmes said in 1927, “Taxes are what we pay for civilized society.” But must we pay even in death? The federal government has a long established set of wealth transfer taxes designed to pay back the government for the protection it provided to a decedent during his or her accumulation of wealth. One such tax is the federal estate tax which is imposed on decedents whose estates are valued at over $600,000 at the time of death.

You are a newly graduated associate of the Ras, Ma, and Tas law firm that represents the estate of Dealing Don, the late, great Aspen rental real estate mogul. The fair market value of his rental real estate holdings is over $6 million. Your senior partner finds an Internal Revenue Code section that allows a “use” value for family-owned businesses. This use value is intended to preserve family farm ownership. Should you convert these city rental units to agricultural “use” in order to reduce their reported value to under $600,000?

**III. Outline**

# Law and Ethics—ethics is a set of moral principles or values that governs the conduct of an individual or a group. The law may permit something that would be ethically wrong.

# Theories of Ethics

## Ethical fundamentalism—People look to an outside source or central figure for ethical guidelines

## Utilitarianism—People choose the alternative that would provide the greatest good to society

## Kantian ethics—A set of universal rules based on reasoning establishes ethical duties

## Rawls’s social justice theory—Moral duties are based on an implied social contract

## Ethical relativism—Individuals decide what is ethical based on their beliefs about right and wrong

**Ethics**

**Social Justice**

**Theory**

**Deontological**

**Theories**

**Consequentialism**

**Ethical Fundamentalism**

**Utilitarianism**

**Egoism**

**Altruism**

**Consequences**

**Professional Ethics**

**Outside Sources**

**Reasons**

**Fairness**

**Ethical**

**Relativism**

**Individual**

**Beliefs**

# Social Responsibility of Business

## Social responsibility of business is a duty owed by businesses to act socially responsible in producing and selling goods and services

# Theories of Social Responsibility

## Maximize profits

### To maximize profits for stockholders

## Moral minimum

### To avoid causing harm and to compensate for harm caused

## Stakeholder interest

### To consider the interests of all stakeholders, including stockholders, employees, customers, suppliers, creditors, and local community

## Corporate citizenship

### To do good and solve social problems

# Examples of Ethical Questions

## Is it ethical to pay bribes in a foreign country where that is the common business practice?

## Is it ethical to use cartoon characters to advertise cigarettes?

Is it ethical to pollute legally if there is another way to handle the problem?

Is insider trading appropriate?

Should working conditions in another country be changed to mimic our standards before we buy products manufactured in these countries?

Methodology

Identify all alternatives

Identify all stakeholders

How do all alternatives affect all stakeholders?

Choose ethical theory

Decide

Sarbanes-Oxley Act prompts companies to adopt a code of ethics.

**IV. Objective Questions:**

**Terms:**

1. A theory that says law should be based on morality and ethics is called \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

2. When a person looks to an outside source for ethical rules or commands, he or she might be categorized as a \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

3. A moral theory which dictates that people must choose the action or follow the rule that provides the greatest good to society is called \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

4. A moral theory which says that people owe moral duties that are based on universal rules is called \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

5. Basing one's behavior on the adage: "Do unto others as you would have them do unto you" is called the \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

6. A moral theory that says each person is presumed to have entered into a social contract with all others in society to obey moral rules that are necessary for people to live in peace and harmony is called a \_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_.

7. A theory of social responsibility that says a corporation must consider the effects its actions have on persons other than its stockholders is called \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

8. A theory of social responsibility that says a business has a responsibility to do good is called \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

9. Under the traditional business judgment rule, directors of a corporation owe a \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ to act on an informed basis, with reasonable care, and in good faith.

10. This act generally makes it a crime for U.S. companies to bribe a foreign official for purposes of conducting business. It is called the \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ Act of 1977.

11. The Houston-based energy company noted now for a major ethical scandal is \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

**True/False:**

1. \_\_\_\_ Under Kantian ethics, morality is judged by a person's act or motives.

2. \_\_\_\_ Moral Minimum is a theory of social responsibility that says that business is responsible for helping to solve social problems that it did little if anything to cause.

3. \_\_\_\_ Law and ethical standards never conflict with one another. If something is a law, it is, by definition, ethical.

4. \_\_\_\_ Company codes of ethics are a form of Ethical Fundamentalism.

5. \_\_\_\_ Under Ethical Fundamentalism, a person looks solely within himself or herself for ethical codes or commands.

6. \_\_\_\_ Immanuel Kant would support the Golden Rule.

7. \_\_\_\_ John Locke and Jean Jacques Rousseau would support the Social Contract theory of morality.

8. \_\_\_\_ Ethical Relativism has been widely adopted as a moral theory because of its strict guidelines.

9. \_\_\_\_ A corporation which moves jobs overseas to take advantage of lower pay scales is adhering to the Stakeholder Interest school of corporate ethics.

10. \_\_\_\_ Social audits are now the norm in the corporate arena.

**Multiple Choice:**

1. Literal Larry believes that all ethical standards and rules are set out in a book called *Ethics For All* that was written by a prominent ethical theorist. Larry refers to this book for guidance and rules by which to lead his life. Which of the following moral theories most accurately describes Larry's conduct?

A. Kantian Ethics.

B. Utilitarianism.

C. Ethical Relativism.

D. Ethical Fundamentalism.

2. Societal Sarah believes people should take actions that benefit society as a whole the most. Which of the following moral theories most accurately describes Sarah's beliefs?

A. Kantian Ethics.

B. Utilitarianism.

C. Rawl's Social Justice.

D. Ethical Fundamentalism.

3. Individual Ingrid firmly believes that each person must look at her own feelings of what is right and wrong to decide what is ethical. Which of the following moral theories most accurately describes Ingrid's beliefs?

A. Utilitarianism.

B. Ethical Fundamentalism.

C. Rawl's Social Justice.

D. Ethical Relativism.

4. Dutiful Daisy always considers how she would feel in another person's place before she takes any action. Then, Daisy only acts in accord with how she would want others to behave in the same circumstances. Which of the following moral theories most accurately describes Daisy's conduct?

A. Kantian Ethics.

B. Ethical Relativism.

C. Ethical Fundamentalism.

D. Utilitarianism.

5. Fair Fran believes that fairness is the essence of justice. In addition, Fran believes all people in a society have a contract with one another to obey moral rules. Which of the following moral theories most accurately describes Fran's beliefs?

A. Utilitarianism.

B. Ethical Fundamentalism.

C. Rawl's Social Justice.

D. Ethical Relativism.

6. C.E.O. Ceo believes her corporation must consider what effects it may have on its employees, suppliers, customers, etc. Which of the following social responsibility theories does Ceo most likely subscribe to?

A. Corporate Citizenship.

B. Stakeholder Interest.

C. Moral Minimum.

D. Maximizing Profits.

7. C.E.O. Crusader believes his corporation can be influential and should be responsible for helping solve many social problems. Crusader believes his corporation should address problems above and beyond those actually caused by the corporation. Which of the following social responsibility theories does Crusader most likely subscribe to?

A. Corporate Citizenship.

B. Stakeholder Interest.

C. Moral Minimum.

D. Maximizing Profits.

8. Advocate Andrew believes corporations should not only be held accountable for their financial states, but also for some level of social responsibility. Andrew's beliefs would most likely be defined as:

A. A code of ethics.

B. A social contract.

C. A corporate social audit.

D. A distributive justice theory.

9. Corporate codes of ethics can be derived from principles educated by:

A. Ethical Fundamentalism.

B. Utilitarianism.

C. The Categorical Imperative.

D. All of the above.

10. Nobel Prize winner Professor Emeritus Milton Friedman would favor a corporate code of conduct that would:

A. Maximize profits at all costs.

B. Maximize profits based on open and free competition.

C. Maximize profits as long as the corporation plays within the rules without fraud or deception.

D. B and C only.

**V. Answers to Objective Questions:**

**Terms:**

1. *Moral theory of law*. Without it, law has no foundation.

2. *Ethical fundamentalism*. The Natural Law School of jurisprudence is considered to be one of the oldest, and it is still quite important in the study of law and ethics.

3. *Utilitarianism*. Many people have difficulty with this theory because of its lack of absolute or bottom line standards.

4. *Duty ethics*. This is traceable to religious doctrines.

5. *Categorical imperative*. The key advocate was Kant.

6. *Social contract*. Many of the newer schools of jurisprudence are variations on this basic theme.

7. *Stakeholder interest*. The difficulty lies in defining who is a stakeholder.

8. *Corporate citizenship*. This debate has gone on since the inception of the corporate form.

9. *Fiduciary duty*. It is the highest standard of duty implied by law.

10. *Foreign corrupt practices*. Note, the payment may be legal if it was lawful under local written laws of the foreign country where the payment was made.

11. *Enron Corporation*. At the time, Enron was the largest company in America ever to file for bankruptcy.

**True/False:**

1. True. The test is based on the categorical imperative.

2. False. Moral Minimum is a theory of social responsibility which says that corporate social responsibility is to make a profit while avoiding harm to others. Corporate Citizenship is a theory of social responsibility that says business is responsible for helping to solve social problems that it did little if anything to cause.

3. False. The law may be contrary to a person's ethical standards.

4. True. The real question is whether they are being enforced or whether this is just the latest form of public relations.

5. False. Just the opposite is true. Under ethical fundamentalism, one looks to an outside source. This source may be from religious or political teachings and the like.

6. True. The Golden Rule is generally accepted as being based on the categorical imperative preferred by Kant.

7. True. Under this theory, there is an implied contract which states: "I will follow the rules if everyone else does."

8. False. Even though ethics remain an extremely personal decision, few people deny that some universal ethical rules should apply to everyone.

9. False. Most proponents of this school of thought would argue that such a move is based on the shareholder's interest alone.

10. False. In spite of the enlightened self-interest which can arise from checking for safety and environmental and consumer protections, social audits are still the exception, not the rule, on the corporate scene.

**Multiple Choice:**

1. D. One of the key criticisms of any form of fundamentalism is that it tends to be too simplistic by trying to answer all questions at all times.

2. B. This approach tends to balance the various interests involved and weigh in favor of the most benefit possible for the least social cost or harm.

3. D. Many people have difficulty with this theory because of the lack of outside controls on

Ingrid's decisions.

4. A. This theory is also often referred to as the Golden Rule.

5. C. This theory represents one of the newer schools of jurisprudence.

6. B. The debate goes on as to how big the stakeholder class should be.

7. A. Most corporations have only bought into this theory on a limited basis.

8. C. A corporate social audit, in theory, would hold a corporation accountable for its social responsibility as well as its financial status.

9. D. All of these theories can and do provide rational bases for guidelines which can be used in a corporate code of ethics.

10. D. Professor Friedman holds the traditional view that the social responsibility of business is to serve its shareholder first through profits lawfully gained.

**VI. Answers to Essay Question:**

A tax law practitioner has a duty to represent his or her client in an ethical manner as prescribed by the professional canons of ethics. For example, candidates for admission to the bar swear to “not counsel or maintain any suit or proceeding which shall appear to be unjust, nor any defense except ... to be honestly debatable under the law of the land.”

The behavior expected here would be to use all *legal* arguments to favor your client’s position. This would include any reasonable interpretations of Internal Revenue Code sections that may be applicable in the case at hand.

The law firm should affirm maximum advocacy for its client, but guard against unethical behavior that would pervert the true intention of this code section, i.e., it cannot make white black or vice versa only to save taxes. If there is no plausible way these parcels could be used as agricultural properties, you and the firm should ethically advise your client against using such an IRC code section in this case.

Perhaps, some earlier estate planning should have been done to prevent this problem. In any event, the present tax problem must be ethically dealt with by legitimately arguable positions regarding the code sections involved.

The bottom line rests within ourselves. We all have a duty to pay taxes. These taxes can be avoided legally and ethically. They cannot, however, be evaded by specious claims not based in any sort of reality. In order to help this process an analysis should include reviewing how all the alternative courses of action might affect all the possible stakeholders, including ourselves and society as a whole. In the end, we must develop our best personal instinct to draw the bottom line, but also to do so ethically.