BUSINESS & SOCIETY

PERSPECTIVES ON ETHICS & SOCIAL RESPONSIBILITY

HAY, GRAY & SMITH

3D EDITION

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PERSPECTIVES ON ETHICS & SOCIAL RESPONSIBILITY

THIRD EDITION

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PREFACE

We wrote this book, including text and cases, along with selection of cases of other authors, to help students to prepare to deal with social issues during their lifetime. In our opinion, if future leaders of business are to improve the quality of life for society, they need to be aware that businesses not only have an economic mission but that these businesses can also contribute to a solution of some of the social problems confronting our country. If improving the quality of life is to be meaningful to future business leaders, then they need to appreciate some of the responsibilities of businesses in order to solve some of the pressing noneconomic and economic problems that have evolved recently. As authors we are convinced that a business, to be socially responsible, must pass a four-way test: (1) meet its economic responsibilities, (2) obey the laws of society, (3) be ethical in its dealings with stakeholders, and (4) voluntarily tackle some of the problems of society in general.

A major portion of this book is devoted to the concept of ethical behavior. If one accepts the notion that ethics deals with "right" and "wrong" standards of behavior that are determined by the ethical and social expectations of society in general, then we can expect responsible people to observe some of the ethical standards of our society. We are of the opinion that some of these "right" and "wrong" ethical behaviors may be stated as follows:

Ethical Standard	**"Right"**	**"Wrong"**
Honesty	Tell the truth	Lie
Integrity	Keep your promise	Break your word
Fairness	Treat people equally	Discriminate
Service	Help people	Exploit people
Concern for life	Life is sacred	Harm people

Many of the cases in this book have ethical overtones. These cases are scattered throughout all the chapters. The ethical issues involve trade-offs among ethical decisions and economic, legal, political, social, and cultural concepts.

It is doubtful in our minds that these cases will change student behavior, but the cases should make the student aware of ethical issues in contrast to other issues. We are firmly convinced that the ethical responsibilities are one of the four-way tests to determine a socially responsible organization as well as determining a socially responsible person.

Our rationale for developing the text and cases was first to have students become aware and understand the definition of a socially responsible organization, followed by a recognition of the determinants of strategy formulation for social strategies. We want to show how the CEO's philosophy pervades the perception of the quality-of-life objective, an assessment of the external environment, the organization's resources, in determining a strategic fit for a social issues strategy. Then we wanted to expose students to governmental relationships and their problems as well as make future leaders recognize some of the ethical decisions facing them. After that we wanted to address some voluntary actions a business might want to pursue in dealing with pollution problems, consumerism, and employee quality-of-life problems. Finally, we want students to understand how to implement social issue strategies and how to measure (at least qualitatively) whether the organization is accomplishing its social responsibilities to achieve the quality-of-life objective we think any firm should strive to accomplish.

What we hope to accomplish is to have students make value judgments about various issues through the case method. Consequently, we have included short, medium, and long cases to illustrate the concepts in the textual material. This book is to be a supplement to other course material in a typical business and society course.

We have included current material ("hot" topics) in the cases, such as Judge Bork's decision regarding women's rights in the workplace, apartheid in South Africa, an unethical situation in college football, toxic waste, Lee Iacocca's odometer problem, the case of the Ford Pinto (from a Ford executive's perspective), and sexual harassment. We have tried to make students integrate their knowledge of accounting, statistics, human behavior, marketing, production, economics, political science, sociology, psychology, and other courses into some of the cases in the book.

Questions at the end of the chapters are included to ensure that students grasp the material in the textual portion. Most of the questions at the end of the cases are used to get the students to address the issues in the case. Additional references are presented at the end of chapters (some new, some old) if additional reading is required. For instructors who prefer to compare their "solutions" with the authors', a teaching manual is also available.

This third edition represents a major revision of the previous two editions. Based on our research, we have added five new chapters. Chapter 2 deals with the determinants of strategy formulation. Chapter 4 deals with the concept of ethics. Quality of life for employees is in chapter 7. Chapters 8 and 9 deal with implementation of social strategies. These are subject matter areas that are crucial to corporate social responsibility. These five chapters were not in the first and second editions except as incidental topics.

To keep current we have added more than 40 new cases and retained about 20 more classic cases. The new cases have been researched and gathered since the second edition was published. We have tried to present a variety of short, medium, and long cases, most of which deal with issues facing medium-sized and big businesses.

The authors feel comfortable with the textual material and the cases in this edition. Since 1973 we have researched and written cases and presented some of the longer cases to the North American Case Research Association (formerly the Southern Case Research Association). Our peers have reviewed some of the more complex cases, and some have been published in other places. In addition, we have directed doctoral dissertations in the area of social responsibility, performed research with businesses regarding the topic, and conducted seminars in the area. We assume responsibility for the material, cases, and cases selected of other authors. We hope you will enjoy this edition of the book.

Robert D. Hay
Edmund R. Gray
Paul M. Smith

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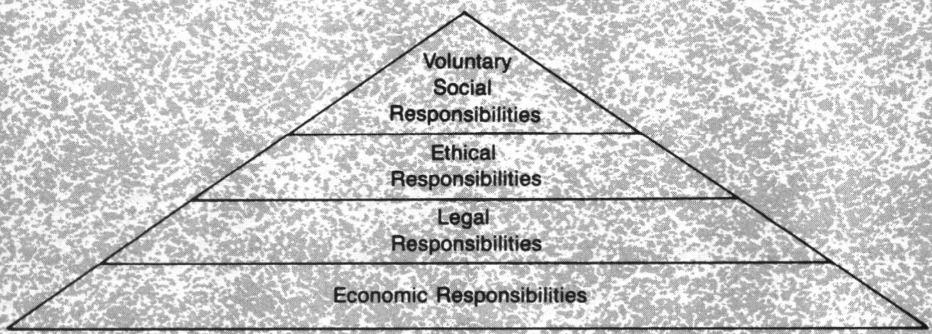
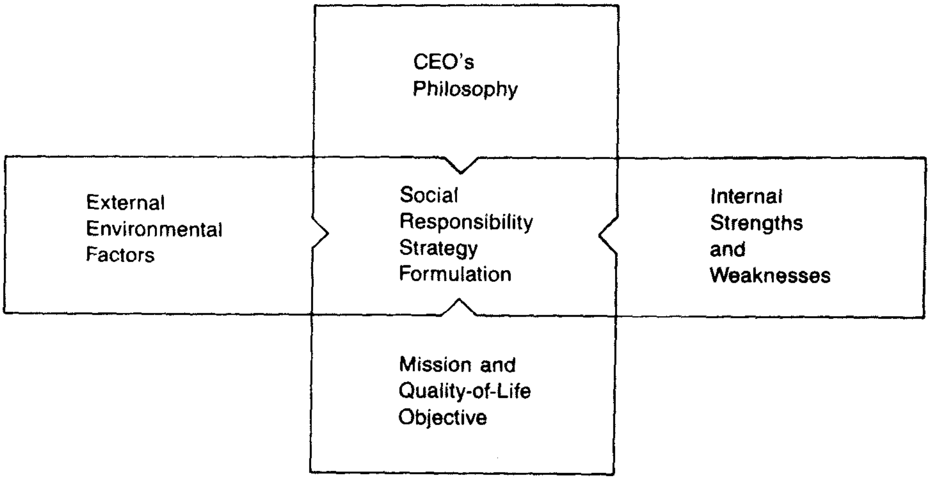
PART ONE

INTRODUCTION

To fit the definition of *corporate social responsibility,* a company must pass a hierarchy of four tests: (1) the organization must first discharge its economic responsibilities, (2) it must obey the laws of the land, (3) it must be ethical, above and beyond the law, and (4) it must voluntarily attempt to meet the expectations of society. These four tests, depicted in the accompanying figure, are discussed in chapter 1.



Chapter 2 presents some determinants of strategy formulation regarding social issues. There are at least four determinants of strategy formulation. The first is the philosophy of the administrator who perceives a possible social issue. The second is the resulting economic mission and related quality-of-life objective of the organization, usually determined by the administrator's philosophy. The third is the administrator's perception and appraisal of the internal strengths and weaknesses of the firm. The fourth is the administrator's perception and appraisal of the external uncontrollable factors, both economic and noneconomic. There may be others, but these four usually determine the overall purpose and quality-of-life objective and the related strategies of the organization. These four determinants provide the strategic fit of the social responsibility strategy formulation as shown below.



C H A P T E R O N E

INTRODUCTION TO SOCIAL RESPONSIBILITY

Congratulations! You have recently graduated from college with a business degree. For the past year, you have been manager of the Human Resources Department for a firm that has two thousand employees. You have just been ordered to lay off three hundred assembly line workers because an economic downturn resulted in decreased orders for the product your firm produces. You ponder. Should you make cuts in accordance with seniority? Should you make a special effort to retain minorities and women whom you hired this last year after you attended a seminar on equal employment opportunity? What should you do? What will you do?

Your recent degree in business and course work in Spanish enabled you to obtain a position in international sales with an agricultural chemical firm. The U.S. Environmental Protection Agency has banned one of your firm's products because it is suspected of causing cancer. The ban does not apply to foreign sales. Should you accept a $50,000 order (your commission is $2,500) from a dealer in Mexico, where they are more worried about ruined crops than about the risk of cancer? What should you do? What will you do?

Your degree in accounting with a minor in real estate has enabled you to get a job with a major property management corporation. Your supervisor has asked you to appraise a parcel of real estate owned by a client at a higher value than you think appropriate. Should you render the higher appraisal or stick to your original estimate, thus incurring the disfavor of your supervisor? What should you do? What will you do?

The purpose of this book is to give you information to help you to make informed decisions (that is, decisions that will narrow the gap between what you "should" do and what you "would" do) in these and similar situations. Read on and enjoy!

This chapter is divided into the following parts:

1. some aspects of the business-society interface,

2. a brief history of business-society relationships,
3. a definition of business or corporate social responsibility,
4. a rationale for business social responsiveness,
5. the direction of the remainder of the book, and
6. a chapter summary.

THE BUSINESS-SOCIETY INTERFACE

The word "society" refers to an enduring and cooperating group of people whose members have developed organized patterns of relationships through interactions with one another. A society might comprise a community, nation, or other broad group of people having common institutions, collective activiities, and interests. The word "institution" typically refers to a social organization such as a church, school, court, or level of government.

One important social institution in the United States (and in most developed countries of the world) is business. The purpose of business firms is to produce and distribute goods or services for a profit. According to the *1986 Statistical Abstract of the United States,* the 1982 income tax returns filed by business organizations in the United States showed the following:

	Number*	Revenues#	Net Income#	Wages Paid#
Proprietorships	10.1	$ 434	$ 51	$ 46
Partnerships	1.5	297	7	23
Corporations	2.9	7,024	198	1,198
Total	14.5	$7,755	$256	$1,267

*Millions of firms
#Billions of dollars

Clearly, the corporate form of business wields more power in terms of revenue generation (corporations generated 90 percent), net income earned (76 percent), and wages paid (95 percent) than the other forms of business organizations in the United States. In fact, the concentration of power by the top 450 revenue-producing corporations shows that they generated 73 percent of the revenues ($5,680 billion). Because of the social and economic impact of corporations, many people use the terms "business social responsibility" and "corporate social responsibility" interchangeably. In this book the society to be discussed is the people of the United States. The businesses to be treated will include incorporated and unincorporated firms.

Within any society, institutions (businesses, courts, various levels of government, churches, schools, etc.), groups (households), and individuals interact. Sociologists aver that as societies become more complex, intradependence increases, taking the form of more numerous and penetrating interfaces among components such as businesses, levels of government and other institutions, households, and individuals. In other words, each component is likely to have an increasingly dramatic impact on the others as society becomes more complex. An illustration of intradependence in a society is the case of a major manufacturing firm suddenly closing. Its former employees suffer diminished purchasing power, which in turn has a negative impact on other retail and service businesses. The tax base of the community, its schools, churches, and other institutions, are also negatively affected. Some communities become virtual ghost towns.

Similarly, there is more interdependence among various societies as they interact about such matters as trade relations, communications, monetary policies, and the flow of labor inputs (through immigration regulations). An example of interdependence among societies is the case of an Arab oil cartel that adopts a strategy that affects the supply and price of petroleum products in the United States. That, in turn, negatively affects the banking system in Texas, which could adversely affect the housing market in Houston. Awareness of the ramifications of interactions like these can help businesspeople avoid making inappropriate business decisions and losing profitable business opportunities.

An essential property of social systems is that they possess values and norms. "Values" may be defined as a broad tendency by individuals and groups to prefer certain states of affairs over others or to share a belief as to how things should be. Within a society, it is possible for one set of values to conflict with another set. "Norms" represent the collective values of groups within the system and hence the shared beliefs of a society.

Organizational (e.g., businesses, legislatures, schools) activities produce consequences that are then experienced by individuals in society. If these consequences conform to the values and norms held by the society, then those activities will be reinforced. However, if results deviate from established values and norms, either the values and norms of society will change, or (more than likely) the organization will be forced by society to change in order to reestablish system equilibrium. It is possible for activities to have mixed consequences. If so, the activities may be tolerated as long as good results outweigh the bad.

One researcher of social systems lists five principles that describe the interaction of organizations with society:

1. Each organization operates at the pleasure of greater society and eventually in the way that society desires.
2. Society's experiences with the results and consequences of an organization's activities help shape future values and norms, which in turn determine the permitted future activities of that and other organizations.
3. Society makes efforts to correct what it doesn't like in each organization.
4. Society prevails over organizations in the long run.
5. Society isn't totally capricious. In fact, it is reasonably predictable.

If these principles describe the real world, then astute managers of organizations should attempt to determine the results and consequences of their organizational activities vis-à-vis the current and future values and norms of society.

A short history of business–society relationships in the United States (that is, managerial and business organization behavioral tendencies interacting with past values and norms of society) shows how business has adapted to changing social values.

A BRIEF HISTORY OF U.S. BUSINESS–SOCIETY INTERFACES

United States business-society interactions may be classified into three major eras or phases: the profit-maximizing phase, the trustee management phase, and the quality-of-life management phase.

THE PROFIT-MAXIMIZING PHASE

Jeremy Bentham, a late eighteenth-century English philosopher, espoused the social, political, and economic goal for society to be "the greatest happiness for the greatest number." That cardinal principle was incorporated into the United States Declaration of Independence as the "pursuit of happiness," and it became a social goal of the American colonists. Bentham's principle was also included in the Preamble to the Constitution of the United States, where the goal was stated as "to promote the general welfare."

The economic and political systems through which early Americans strove to promote the general welfare emphasized the freedom to pursue one's individual self-interests. Adam Smith, an English political economist who wrote in the eighteenth century prior to the industrial revolution, stated that the best way to promote the general welfare (the wealth of a nation) was:

> Every individual is continually exerting himself to find the most advantageous employment for whatever capital he can command. It is his own advantage, indeed, and not that of society, which he has in view. But the study of his own advantage, naturally, or rather necessarily leads him to prefer that employment which is most advantageous to society. . . . By directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for the society that it was no part of it. By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it. I have never known much good done by those who affected to trade for the public good. It is an affectation, indeed, not very common among merchants, and very few words need be employed in dissuading them from it ([1776] 1937, pp. 421-423).

Smith's perception was that in a *competitive* and *laissez-faire* (unregulated) environment, each businessperson would own and manage a small firm, each would act in self-interest (to maximize profits), and the composite behavior of the business community would result in an aggregate benefit to society.

Smith's economic values have had an important influence on United States business thinking. As a result, most businesspeople for the first 150 years of our history embraced the theory that social goals could best be achieved by emphasizing the pursuit of individual self-interests and by attempting to maximize profits. This philosophy is currently held by many businesspeople and is the one espoused by Milton Friedman (1970).

Concurrent with the industrial revolution, the corporate form of business organization developed. Large pools of capital were amassed in order to effectively derive the benefits of specialization and realize the technological potential of mass production techniques. The power of the corporation to affect society increased dramatically. What would be the social impact of the corporation?

Though far-sighted, it is questionable that Adam Smith could have visualized the concentration of power and resources that has been amassed using the corporate form of organization. Smith, though, did admit that whenever owners of businesses (small or large) meet, a conspiracy to fix prices and other nefarious behavior to eliminate competition is likely to ensue ([1776] 1937, pp. 66, 128) and, if the private sector of the economy is incapable of coping with societal ills resulting from such behavior, then the public sector should act (pp. 734, 735, 768).

Karl Marx, in *Capital*, predicted that an increasing concentration of power to affect society would reside with capital-intensive business firms, that labor would continually be exploited, and that the outcome would be worker revolution, which would lead to a reformation of society in which the state (national government) would take ownership of large and, perhaps, small business firms.

Neither the Smith nor the Marx prediction about corporate impact was completely congruent with the United States experience, though that of Adam Smith came closest. The United States society in the nineteenth century was one in which there was a relative shortage of productive capacity. The legal and political emphasis was on protecting and nurturing infant industry; economic growth and the accumulation of aggregate wealth were the primary goals. The business sector with its emphasis on maximum profit was seen as the vehicle for achieving those goals. In the process, abuses of employees such as child labor, starvation wages, and unsafe working conditions were tolerated. No questions were asked about the misuse of resources such as timber, soil, and minerals or of abuses to the environment (air, water, and land pollution). Nor was there meaningful concern about urban problems, unethical advertising, unsafe products, or minority group problems.

At the close of the nineteenth century, however, rumblings of discontent began to be heard. Unsafe food-processing practices and the manufacture of impure pharmaceutical products led to the passage of the Food and Drug Act of 1906 and the eventual establishment in 1931 of the Food and Drug Administration. Perceptions of corporate misuse of power by trusts to eliminate competition and influence public policy led to the passage of the Sherman Anti-trust Act of 1890 and the eventual establishment of the Federal Trade Commission in 1914. The duty of that agency is to regulate competition among firms so as to ensure that no one firm becomes too dominant or powerful. However, even though Congress passed food and drug and antitrust legislation, during the first thirty years of the twentieth century the laws were not enforced.

THE TRUSTEESHIP PHASE

In October 1929, the stock market crashed, heralding the Great Depression in the United States and other developed economies. Massive unemployment occurred, factories were idle, and distribution of goods and services became erratic. The major institutions of society (business, government, academe, church, and the family) and their relationships were scrutinized and reevaluated. Many felt that Smith's invisible hand had lost its grip and that the emphasis on the business owner's self-interest was too predominant because it seemed to operate at the expense of other contributors to business organizations. Thus evolved a philosophy of management based on the premise that social goals would be achieved by balancing the interests of several groups of people who had an interest or stake in the business organization. These groups are referred to as "stakeholders" or "constituencies"; they typically include consumers, creditors, the community, government, owners, managers, employees, suppliers, and society.

Impetus was given to the stakeholder philosophy by 1930s New-Deal federal legislation designed to relieve the distress of businesses, employees, farmers, consumers, investors, homeowners, and other groups from the economic imbalances resulting from market abuses or failures. Some examples of this legislation are the Securities Exchange Act of 1934 (prescribed information that must be provided to investors and potential investors), Wagner Act of 1935 (prohibited unfair labor practices by employers), Civilian Conservation Corps Act of 1932 (provided for youth employment), Federal Emergency Relief Act of 1932 (federal funding of state welfare programs), Agricultural Adjustment Act of 1933 (agricultural price supports), Glass-Stegall Banking Act (bank depositor's insurance), Reconstruction Finance Corporation Act of 1932 (government credit to aid financially troubled businesses), Social Security Act of 1935 (worker retirement system), and Fair Labor Standards Act of 1938 (minimum wage for covered workers and regulation of child labor).

Other forces prompted the emergence of the trustee-constituency view of business social responsibility. Two of these were the increased diffusion of ownership of the shares of United States corporations and increased pluralism in our society.