CHAPTER 4.

THE IMPACT OF ETHICS ON BUSINESS.

“VERY FEW EXECUTIVES ARE OUTRIGHT SCOUNDRELS. RATHER VIOLATIONS OF CORPORATE AND SOCIAL VALUES USUALLY OCCUR INADVERTENTLY BECAUSE NO ONE RECOGNIZES THAT A PROBLEM EXISTS UNTIL IT BECOMES A CRISIS. THIS TENDENCY TOWARDS INITIAL TRIVIALIZATION SEEMS TO BE THE BIGGEST ETHICAL PROBLEM IN BUSINESS TODAY.”

Laura L. Nash
Ethics without the Sermon.
Harvard Business Review on Corporate Ethics.
(35. Harvard, 2003: 30)

Before discussing ethics and business it is necessary to agree on the role of business in society, ethics having received our attention in the previous chapters.

It is said that the purpose of business is to make profits. Without profits, no one would invest or remain invested in a business; it would slowly collapse, and, instead of being a job creator, it would destroy work places. Profitability must, however, be of a long-term nature (see also chapter 3 Sustainable Development). A one-year profit explosion and thereafter liquidation is not of much help to the shareholders, employees and society at large.
Business has different moral duties from those of the individual. It has, among others, the moral duties to survive, to earn profits and to create long-term wealth because that is what gives it its right of existence and that is the purpose for which it was created. Only by earning profits will the business be able to fulfill its other ethical duties towards its stakeholders and society at large, e.g.:

- To create livelihoods – jobs;
- To supply goods and services wanted by the market;
- To contribute to the health and growth of the economy;
- To pay taxes;
- To respect the dignity and autonomy of all persons;
- To comply with its responsibly designed ethics, corporate governance and sustainable development policies;
- To help develop institutions (engage government, NGOs and other relevant bodies);
- To create a healthy and motivating work environment and
- To support – within its means and subject to approved budgets – charitable organizations, social efforts such as education and training, the arts, sport etc.

With the exception of Marxism, all ethical theories, as quoted earlier in this report, fully supports the morality of the profit motive as long as it is not profit at any price and as long as it is a reasonable profit. Competition, the free market system, is there to help ensure through the pricing mechanism that profits remain within boundaries acceptable to society. For these reasons monopolies, oligopolies, price fixing and other anti-competition behaviour are unacceptable and governments have the duty – through competition boards or similar instruments – to prevent their development.

Sound businesses are the basis of a healthy economy, which is to the advantage of most. Thus utilitarian theory supports the right of business to earn market related profits. Kantian theory also accepts this business role as a moral duty provided business upholds the provisions of the categorical imperative (see page 11) in pursuing profitability. Because business has as its function the provision of goods or services to society at a
profit, virtue ethics would accept this function as business’s distinctive “craft” and thus as a virtue of business. This would be subject to business complying with the doctrine of the mean (see pages 19 and 21), i.e., profits need to be reasonable, market related and earned in an honest manner, by a virtuous character (business).

You may well say that this sounds all very theoretical, idealistic and a little naïve. And it is true that in the tough world of business with its cut and thrust competition and the fight for survival, ethics, which concerns itself with practical reasoning about good and right, about duty and obligation, about virtue and freedom, and about rationality and choice, is frequently viewed by so-called hard businessmen in a cynical light. It is sometimes considered weak and unintelligent to act in an ethical manner. This thinking seems to me to emanate from times when businesses were run in an authoritarian manner, when the boss laid down what was to be done and employees carried out his instructions without daring to ask a question or even make a suggestion. It probably also stems from a misunderstanding of what is meant by “ethics in business”. Sensible businessmen have long ago accepted that ethics and sound business need to complement one another. But it is self evident that ethics can play a meaningful role in business only if it helps to build and sustain a better enterprise.

Contemporary circumstances require an approach to ethics very different from that of the authoritarian, old fashioned businessman. Due to:

- The vastly greater complexity of business;
- The advance of technology which revolutionizes our lives;
- The much greater speed with which business has to be conducted;
- The much longer distances over which business has to be transacted;
- The much greater fragmentation of ownership;
- The far more competitive environment;
- The much larger scale of business;
- The massive information flows that need to be handled;
- The pressing ecological questions and problems;
- The problem of knowing the future effects of new technologies on our lives;
The need for the humanization of the workplace;
The complications involved in dealing with growing unemployment;
The ever increasing pressure by society for business to deliver real value, to be socially responsible and to protect the environment and
The large number of laws and regulations

business has become far more intricate and complicated to manage and administer. At the same time, people’s options to act constantly increase and the demand for specialist knowledge and intelligence also grows. The owners, directors and/or managers of a business can no longer be expected to know everything or be everywhere. Subsidiarity needs to be employed in order to provide motivated, efficient and personalized service to the market. It is therefore impossible for the owners, directors and managers alone to dictate what is to be done and so they must delegate if they want the business to remain competitive. But effective delegation requires careful selection of the persons concerned, who must be trusted, respected, motivated and given the necessary responsibility and authority to act (their dignity and autonomy – in Kant’s language – must be protected). Ethics can be an effective tool to help in achieving successful delegation.

Although our world has become much more individualistic, we have become considerably more dependent on others. No one, and certainly no business, can function entirely in isolation. Without customers, suppliers, employees, shareholders, accountants, lawyers and so on, a business could not function. It is therefore vital to the businessman - in all his decisions and actions - to keep others in mind. Should he deal with others in an authoritarian, uncaring, off-hand manner, riding roughshod over their interests and needs, he may reap the same in return, which is clearly not in the interest of his business. No business can rely on an authoritarian business style; all decisions must take others into consideration. Business totally depends on and is imbedded in society. That is so not only because business has to supply goods and services to members of society in order to exist and succeed or because it has to attract members of society to become its employees, but also because society is providing the infrastructure that makes it possible for a business to operate. Without the required transport-, legal- and communications- infrastructure, without taxation and political etc. systems, it would be virtually impossible to run a
business. Business pays taxes and fees for these services but it is questionable whether they compensate society sufficiently (see also chapter 3 – sustainable development) and in any case they alone do not make for a good interdependent relationship that is so necessary for both business and society to flourish. Consumers may boycott a business’s products and services if society perceives the business to act unethically or not to behave as a good corporate citizen. This raises the question for internationally operating organizations whether that which is considered ethical in one country is moral in another. This problem is discussed in chapter 5 dealing with Cultural Relativism.

As the Shell Brent Spar case\(^{28}\) has shown, it is not sufficient for business to act legally. It must also be seen to be conducting its affairs in a morally legitimate manner. Such moral behaviour has to be seen as an honest, thought through corporate effort, in order to be taken seriously and for it to have long-term positive affects.

While no business can operate without being confronted by ethical issues, there are no ready norms or formulae that can be easily introduced into business and which then automatically produce the required ethical results. Both Kant and Aristotle said that ethics can provide only guidelines, no absolute rules. Business is an entirely practical occupation which must operate in a highly competitive environment and long-term profitability is essential. Because ethics is concerned with the goodness of the interaction between a “self” and “others,” the “self” cannot be excluded from ethics. It is therefore incorrect to neglect the “own” interest – or that of the business. The business’s well-being is a prerequisite for its balanced, ethical interaction with others. Business ethics must aim to align ethics with the organizational goals in such a way that the own interests are balanced with those of all the stakeholders. Keeping this in mind, as well as the fact that people/businesses cannot operate on their own, it seems clear that the ethics of the businessman must be a combination of doing what both serves his long-term interest

\(^{28}\) The Brent Spar which was a very large floating oil storage and loading buoy in the North Sea was decommissioned in 1991 and it was Shell’s intention after very careful investigation to sink the platform. Although Shell complied with all the relevant legal requirements and obtained the British government’s approval for its intended action, it omitted to discuss the matter with the appropriate NGOs. Green Peace on hearing of this plan objected strenuously and the whole affaire became a major environmental and morally charged issue to the serious embarrassment and detriment of Shell and its shareholders.
while ensuring that most others involved with the business are not adversely affected. For a business, making a market related profit is a moral duty and while it may also be management’s wish to produce profits, the overriding motivation for profitability is no doubt business’s obligation to be profitable (I am obviously not talking here of organizations “not for profit” – they would have other duties). As long as the businessman complies with the provision of the categorical imperative while acting to earn such a profit he is acting ethically correct according to Kant’s moral theory. Any ethic that does not also support this drive for the achievement of own interest would be stillborn. Ideal or purely theoretical ethical answers that cannot be converted into reality are of little help. No owner or manager can afford pursuing naïve morality.

It is interesting to note what Adam Smith (the influential Scottish philosopher and economist (1923 – 90)) had to say: “It is not from the benevolence of the butcher, or the baker, that we expect our dinner, but from their regard to their own interest”. Smith was not an admirer of unadorned selfishness. He thought benevolence praiseworthy and a great virtue. He believed that civilized conduct is built on the good character, on sympathy towards others. Benevolence is not required in order to advance the economy and thus the public good. Benevolence is a desire for the good of others and a disposition to act so as to further the good; it has to do with fairness, emotional capacity and is sentiment based. Kant holds that we must at least give some support to those in need. He rejects a policy of refusing to help the needy, but caring for others and supporting them is an imperfect duty (see page 17). A duty that allows leeway in the interest of inclination, i.e., that permits one to choose among several possibilities of fulfilling such a duty. For instance one could choose to help the sick, the starving and one could decide how to help the chosen group. Imperfect duties are usually overridden by perfect duties but must at least sometimes be complied with. A business can neither help all in need nor usually provide a chosen group with all manner of possible relief. A business’s moral duties are those spelt out on page 42 and its morality does not depend on any one of them but on its best endeavours to comply with all, or at least most of these obligations. Consequently, while benevolence by business has positive moral value (if done from the right attitude and with the concurrence of those who actually own the asset that is given away in a
charitable gesture, i.e. the owners/shareholders of the business) it is not an absolutely necessary ingredient of business ethics that a business _always_ acts in a benevolent manner.

The shopkeeper who gives customers certain products below the normal retail price (loss leaders) and does so not for humanitarian reasons but in order to draw customers into his shop where they will hopefully purchase at the same time other goods, on which the shopkeeper makes a handsome profit, does not perform a benevolent act. The shopkeeper’s act is expedient, merely in his own interest. His act would be a benevolent one only if he were to sell certain goods below the normal retail price in order to help others who are in need. Such an act would represent charity, which is obviously good and admirable, but as said before, it is not a sine qua non to ethical behaviour in business.

However, a business which wants to act ethically must at least some times act in a benevolent manner. That is why I believe business should support charities and other worthy social causes via a properly approved budget and should make this part of its board and shareholder supported code of ethics.

Central to any ethic is the relationship of the “ought” and the “can”. Any “ought” presupposes a “can”, i.e. is it possible for a business under competitive pressure to comply with business ethical dictates? Ignoring this question would lead to utopian expectations which would fail in the reality of business and damage the entire case for business ethics. However, whenever one’s own interest, or for that matter those of the business, come into conflict with ethical behaviour, every effort needs to be made to find a way in which both can be brought together resulting in a fruitful solution (43. Suchanek, 2001: 2). Any operation that pursues purely its own interest and that clearly violates the interests of those affected by its activities is not a business – it is a crime syndicate (42. Rossouw, 2002: 25).

As Charles Handy, the well known Irish writer, broadcaster and teacher, wrote in the *Harvard Business Review*: “The purpose of business is not to make a profit per se – it is
to make a profit so that the business can do something better, something that is the real justification for the business”. For me such justification should be for the business to comply with its ethical duties listed on page 42 in addition to striving for survival and the creation of long term wealth. I believe that these ethical duties, including the duty to generate profits, are interdependent – they produce a win-win situation. The European management writer Arie de Geus argued: “Companies die because their managers focus on the economic activity of producing goods and services” (and I would add making short term profits, which efforts have many a time lead to fraud and misrepresentation by management) “and forget that their organization’s true nature is that of a community of people”. Kant’s Kingdom of Ends, as referred to in his categorical imperative, says much the same.

It should be noted here that business ethics is not the same as prudence. Prudence means to be careful so as to avoid undesirable circumstances; it is essentially selfish. Acting in a prudent way may lack moral merit or be morally wrong. In the same vein, although the law is directly concerned with moral problems, legally correct actions may not be morally acceptable and vice versa, if something is illegal it is not necessarily immoral.

Often an important tension in business is between the desire for excessive profit (greed) and morality. Thomas Hobbes, the British philosopher (1588-1679) said about human greed that there is no end goal, only a limitless “wanting more” moving us from one aim to another – the continual progress of the desire (5. Hobbes, 1988). While human ambition is good in so far as it drives development, progress and improvement of society’s circumstances, when it becomes avaricious it is destructive. Ethics’ predominant obligation in business is to contribute towards a solution of the conflict between inordinate profit – the constant desire for more - and morality. It must do so in an ethical and at the same time in a practical, implementable way. Milton Friedman tried to answer this question by stating, “the social responsibility of business is to increase its profits” (33. Friedman, 1970). This attitude could be interpreted as a typical ethical
egoistic\textsuperscript{29} stance. Friedman rules out unfairness, coercion and harming others, but he considers solely the interests of the shareholders and ignores the needs of all other stakeholders. Vis-à-vis shareholders Friedman’s position can be seen as Kantian but his ethic is focused too narrowly.

Jukka Kilpi (37. Kilpi, 1998) gives the need for a company to consider all its stakeholders additional force by clarifying the nature and thus the obligations of a company: Businesses lack moral agency on their own. Their moral obligations are determined by actual contractual and legal arrangements, e.g., the memorandum and articles of association and other contracts such as employment, purchase, sales agreements etc. – the company is thus a nexus of contracts. These contractual arrangements make a business into a secondary moral agent, an artificial person. For a secondary moral agent to exist, moral and legal attributes have to be imbued into it. Only natural persons can do this and they do so, for instance, when they agree to establish a limited liability company in order to co-operate through such a company for a particular aim. The rights and obligations are always ascribed by natural persons to a corporation. Without such prescription a corporation would not exist.

Natural persons, by having autonomy can agree to limit their liability by transacting through and making promises via a limited liability company as long as they do not restrict their own as well as others’ autonomy. As representatives of the corporation, natural persons act as the corporation itself but are bound to respect the corporation’s promises. The representatives cannot act as the corporation contrary to the company’s nexus of contracts – that would be illegal and immoral as it would be tantamount to breaking promises.

Due to this constitution a company cannot take the interest of only shareholders into account – the web of contracts (contracts are the medium of promises) requires the

\textsuperscript{29} Ethical Egoism is the theory that the only valid standard of conduct is the obligation to promote one’s own well-being above everyone else’s.
corporation to recognize and respect the interests of all stakeholders because they are all part of the nexus of contracts.

Autonomy is the source of the moral duty to keep a promise and it also allows us to agree to limit our liability by making promises via a limited liability company. But a promise is the moral essence of a contract and because a company is a set of contracts its moral essence is embodied in the set of promises.

To this I would add that there are of course obligations that appear not to flow from a contractual obligation, e.g. to respect the dignity and autonomy of others or protecting the environment, but such duties should be prescribed in the company’s internal conditions of operation, such as the corporate governance, sustainable development and ethics policies. These policies also represent contracts and therefore are ideally part of the nexus of contracts and set of promises that constitute the company.

While natural persons can limit their liability by transacting through a limited liability company, they cannot through this mechanism escape liability for their fraudulent or immoral acts. As representatives of a limited liability company, natural persons have the moral and legal duties to ensure that their company enters into and acts in accordance with legal and moral contracts. This concept has also been highlighted by a recent case brought against AIG, America’s and the world’s largest insurance company, where the CEO of AIG had to relinquish his job because he had been personally implicated in boosting AIG’s reserves by designing and negotiating an “income-statement smoothing” reinsurance contract.

The contracts making up the web (and resulting set of promises) which constitute the company must all be legal and moral contracts and this forces the company to deal with all its stakeholders (not merely its owners) in a morally and legally correct manner.

This expose shows that Milton Friedman’s view that no moral claim can be made on a business except to secure the best return for itself within the law and the ethical customs
of the society within which it operates, is too narrow. Friedman’s view seems an impoverished conception of what people engaged in business ought to do. The various objectives associated with a business being part of and operating within a community are moral obligations which ought also to be complied with by business (see page 42 for a list of such obligations). Management has a duty to safeguard the welfare of the business and this means balancing the various claims of the stakeholders in the business. The owners require growing returns on their invested capital; the customers want goods/services of excellent quality and at reasonable prices; the market wants the business to spend on R & D so that it can supply new, better, more exciting products; staff want higher wages, a congenial working environment, interesting and fulfilling jobs, training and generous fringe benefits; and the community wants business to protect the environment, support charitable organizations etc. In the interest of the survival and prosperity of the business, management must keep the interests of the various stakeholders in balance. All stakeholders have legitimate claims on the business and their fair and even-handed recognition is necessary for a flourishing enterprise. As an illustration of the inadequacy of Friedman’s notion, I would for example refer to what is said in chapter 11 (Marketing and Sales), page 99: It is the credit insurer’s duty to provide a prospective client with all the relevant information, so that the client can decide, in the full knowledge of all the relevant details, what type of policy she wishes to purchase. This is a moral duty with which the insurer ought to comply even though it may not be in the insurer’s shareholders’ explicit interest of maximizing profit.

The dependence of business on others, as referred to in pages 44 and 45, also calls for a wider responsibility of business, one that includes the consideration of the rights and needs of all its stakeholders, not one that is confined to pursuing purely the interests of its owners.

One could be led to believe that Friedman’s statement should lead to a maxim reading something like this: “We (the owners of the business) will support only those actions by the business that will lead to the immediate increase in earnings in order to grow our long term value and we will not allow other social issues to be recognized as responsibilities
of our business.” Such a maxim would not be capable of universalization because ignoring all other social responsibilities would probably hinder the achievement of the purpose of the maxim – the long term growth of shareholder value. This would be so because all the other stakeholders in the business would be disgruntled and thus not give of their best in order to support and grow the business. The maxim would at the least lead to a contradiction in conception. It would also be contrary to Kant’s direction that one should at least sometimes, help others.

Friedman’s approach to the profit/morality problem seems to lack depth because it offers no heuristic for the solutions of the many conflicts that arise every day in business. For example, how should the following be viewed: paying an incentive in order to obtain a lucrative order; selling at huge profits textile goods manufactured by child labour; or developing and producing pharmaceuticals and selling them at a high price in order to recoup in an inordinately short period development costs but thereby making the product too expensive for purchase by poor countries that are in desperate need of the preparation? The opposite of Milton Friedman’s view is, I believe, the Kantian theory which gives morality the absolute primacy and imposes positive duties on business to aid others even at some cost to itself. This means putting respect for persons first and seeing as immoral any business practice which puts money on a par with people.

If one sees a firm purely as a tool to making profits one is acting contrary to the “respect for persons” principle. The “respect for persons” principle or as the categorical imperative states it “always treat the humanity in a person as an end and never merely as a means” requires that a business respects the dignity and autonomy, not only of its shareholders but of all its stakeholders even if treating others in this manner may not result in the maximization of profits. As we have seen earlier, Kant or for that matter any reasonable stakeholder would expect a business to make a market related profit as long as it is earned in an ethical manner. A moral theory which would forbid striving for equitable profits would make no effort to find a win-win solution for the profit/morality conflict and would therefore not find support in practical every-day life. It would be doomed to failure.
The tension for business between the duties to maximize profits and at the same time help others is in reality only an apparent one. Self-regarding (for a business to only do the prudent thing) and other-regarding (for a business to respect and show concern for others) are generally interdependent. Without respecting and caring for its customers, employees, suppliers, shareholders etc. a business will not be able to maximize profits and create long term wealth. Morality tries to set out the way people should live their lives for them to be good lives. It would be peculiar to suggest that this concept should ignore entirely people’s own interests. Morality therefore should be seen as moderate, balancing the stringent view, which insists on strict other-regarding (a maximalist theory which seems harsh and unreasonable) and prudence, which is entirely self-interested (minimalist theory). The moderate view of morality makes a moral life a realistic possibility and allows the integration of the other-regarding with the self-regarding. Kant said getting joy out of an action can rob it of its moral worth. But this is so only if the fundamentals of the maxim on which the agent acts have as its aim joy for the agent herself. Kant strongly supported actions that make people happy, not because such actions have necessarily great moral worth, but because happy people are much more inclined to live a life based on the categorical imperative. As has been shown on page 17, Kant’s formula of the End-in-Itself prescribes, among others, the duty of self-realization which supports the integration of self-regarding with other-regarding. These views apply to business as well.

Investors and the press celebrate the company that produces exceptional profits and such accolades are well deserved provided the excellent results have not been achieved at the expense of ethical conduct. As Peter Drucker (Drucker, 1987) pointed out, business profits are needed because they are the source of capital formation. Business in the modern economy needs a continuously rising capital base to finance growth, technology and R & D demands, social expenditure, the cost of capital and of tomorrow’s jobs. Without profits the business will fail, not be able to act ethically or be a force in the

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30 Respect: to adhere to constraints on what one may do to others, to acknowledge the dignity and autonomy of others.
31 Concern: caring about other people’s welfare.
support for the public good. Sometimes the competitive nature of business is used as an excuse for unethical behaviour towards competitors. However, competition fosters economic growth, fair pricing and quality of service and must therefore be protected from unfair, unethical, damaging action. Markets have expanded enormously both nationally and internationally and their growing diversity can provide much greater choice at reduced costs for all consumers, particularly the poor. But the full benefit of enlarged markets can be garnered only if global markets are not interfered with. If markets are regulated, wealthier nations must not unfairly exploit poor countries. All market players must be subjected to robust competition and consumer protection laws. Unethical, monopolistic or price fixing business practices will undermine justice, growth, improving standards of living and safety and therefore inhibit investment, development and job creation.

On other occasions business maintains that because of competitive pressures it cannot afford to act ethically. An ethical business is transparent and provides complete and truthful information to its stakeholders so that they can choose freely whether to buy the company’s products or services, whether to supply it with products or services, whether to extend credit facilities to it, whether to accept employment by it or whether to invest in it etc. Such openness builds the reputation of and trust in the enterprise which is the basis of sound long-term stakeholder relations and by and large the best source of competitive advantage if combined with business acumen, efficiency, innovation, industriousness and intelligence.

Plurality, the national state’s diminishing ability to guide due to globalization, and the consistently growing complexity of every-day life, forces business to accept the role of moral actor because no one else does or can alone fulfill this role, e.g., the role big business in South Africa has accepted to play in the HIV/AIDS and Black Economic Empowerment issues. Business ethics is therefore becoming a more and more important discipline.

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32 For a discussion on trust see chapter 6.
To summarize, the role of business is to supply the market with goods and/or services required by society and to do so at a reasonable, market related profit. Business must strive to fulfill its other moral duties (as set out on page 42) which will mean that it satisfies society’s legitimate demands on and expectations of a responsible corporate citizen. Ethics has a distinctly positive impact on the sustainable profitability of business, including credit insurance as will be seen from Part II of this report. Good management includes attention to ethics, corporate governance and sustainable development, but they must be applied honestly, intelligently and, in Aristotle’s words, keeping the “mean” in mind. A simplistic, gullible approach will harm the business and damage the credence of business ethics. Institutions – the subject of chapter 6 – are vital tools helping in the effort to act ethically in business. But before addressing that issue, I wish to examine in the following chapter how business should deal with its ethical norms when it has to operate in a foreign society which has cultural rules different from those of the company’s home country.