

FIRST EDITION

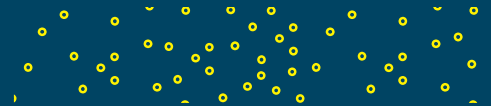
DYNAMIC BUSINESS LAW

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**Mc
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For Review Purposes Only



Part 1 *The Legal Environment of Business*

CHAPTER 1

An Introduction to the Fundamentals of Dynamic Business Law

LEARNING OBJECTIVES

- LO 1-1** Define business law.
- LO 1-2** Relate the functional areas of business to the relevant areas of business law.
- LO 1-3** Recall the purposes of law.
- LO 1-4** Distinguish among types of law.
- LO 1-5** Differentiate between sources of the law.
- LO 1-6** Identify the various schools of jurisprudence.

LO 1-1 Define business law.

This book is for future business managers, especially those who wish to be leaders. An essential factor in preparing for that career is awareness of the legal issues arising in business. Businesses need to finance capital growth, purchase inputs, and hire and develop employees. In addition, they must sell to consumers, please owners, and comply with government rules. All these activities are full of potential legal conflicts.

The conflicts reflected in legal principles and court actions are not simply about abstractions like interests and rights. They are usually about money—who has it, who owes it, and who deserves it. The anger and fear pervasive in legal conflicts affect who has the money at issue at the end of the day. The significance of struggles over money makes it all the more important that business managers learn the basic language of law as soon as possible in their professional training.

A theme of this book will be a surprising number of legal implications that result from what on the surface might look like a simple, everyday business decision. Think along with us about the desire of a young entrepreneur who has a new idea and wants to develop its market potential.

In the seemingly ever-expanding market for smart phone apps, individuals are often rewarded for creating apps that make lives simpler or that entertain people. You have watched the business success of hundreds of smart phone applications. You have certainly downloaded your share of them. You have an idea for a phone app that you believe has the potential to become the next Vine or Instagram.

Your proposed app will allow users to search for lawyers based on the location and specialization that the user desires. The app will also rate different lawyers and provide personal information about the lawyers who are being rated. Your goal is to make it easier for uninformed consumers to locate the lawyer best suited for their needs.

You and a friend, who has a background in computer science, develop software to run the application. You also create a design for the app: what the app will look like and how it will function.

After you complete the design of the app, you decide that you would like to upload it to the Apple App Store. You contact Apple, and a representative tells you that you will be able to upload the app if you pay a fee and sign a few forms.

In this textbook, you will find legal concepts and terms that will allow you to see this scenario with different eyes. What you will learn will warn you about the dangers of letting the excitement of the moment—your big moment—cause you to forget that business is, in part, a series of conflicts. And, in those struggles, you need to understand your interests and responsibilities. From the instant you first interact with another party in a business relationship, insights from your study of business law should kick in to protect you.

Let's walk through just a small sample of the legal issues you will face as you try to make your app the next big thing.

Because you need a platform on which to sell your app, you will need to establish a contract with an app store such as the Apple App Store. This book will teach you about the elements required to establish a legal contract. In other words, only certain kinds of legal agreements will provide legal protection if a later dispute arises. Whether these elements are met will dictate whether the party with whom you are contracting is obligated to perform a certain duty. For example, if you believe that Apple has a legal duty to put your app in its App Store or, perhaps, place your app in a particular position in its online store, you would have to prove that a contract creating such a duty exists.

The knowledge you will gain regarding contract law will also help you understand the complexity of the relationship between you and the user purchasing your app. For example, if the app you created malfunctions after a user has purchased it, how will you and the customer settle a dispute? Will you go to court, or would you prefer disputes to be settled through alternate dispute resolution methods such as arbitration? Will you create a binding arbitration clause to require consumer disputes to be resolved through arbitration? After reading this textbook, you will become more aware of the various conflict resolution mechanisms available to businesses and consumers.

In addition to the contractual issues underlying your app business, you will also need to be aware of possible tort issues related to your app. (A tort, at its simplest level, is legal language for a civil [noncriminal] harm committed against another in which the injured party can sue for damages.) For example, because your app will compare the desirability of certain lawyers to others, the lawyers whom you are rating might feel threatened by your app. Will these lawyers be able to file a suit in tort against you for defamation or privacy torts such as false light or public disclosure of private facts?

Alternatively, what can you do when a competing business writes a column in a newspaper mocking and generally trashing your new app? To answer that question, you need a good understanding of the torts of disparagement or slander of quality, two torts that you might be able to use to defend your business against fraudulent claims. The sections in this textbook on tort law will enable you to ask questions about potential tort claims related to the eventual marketing of your app.

Later, when you market your app, you will also have to be aware of the restrictions on advertising that exist under consumer protection laws. Will you make any promises to consumers regarding your app in your advertisements? Will these advertisements constitute legally permitted puffery, or will they be deceptive advertisements under the Federal Trade Commission Act? As you read about consumer law in this textbook, you will learn about the restrictions the law places on advertising.

When you design your app, you will have to make sure that you do not infringe on the intellectual property—such as patents or trademarks—of other app businesses. What words and symbols will you use? Do those words and symbols constitute trademark infringement? This book will explain the intellectual property law that governs the invention of an app.

Finally, once you have studied this book, you will realize the importance of carefully selecting the form of business organization you and your friend choose for operating this app. For example, will you operate the app under a sole proprietorship or a partnership agreement? As you will learn, each of these forms of business organization provides you with different advantages and disadvantages.

Business law consists of the enforceable rules of conduct that govern commercial relationships (“commercial” meaning “for the purpose of making a profit”). For example, a firm is required by law to obey the antitrust laws when it considers merging with another firm. In other words, buyers and sellers interact in market exchanges within the rules that specify the boundaries of legal business behavior. Constitutions, legislatures, regulatory bodies, and courts spell out what market participants may and may not legally do. These rules and responsibilities provide the stability required in a thriving market economy.

business law

The enforceable rules of conduct that govern the actions of buyers and sellers in market exchanges.

LO 1-2 Relate the functional areas of business to the relevant areas of business law.

Understanding business law is necessary for future businesspeople because there simply is no market transaction that occurs outside legal guidelines. All contracts, employment decisions, and payments to a supplier are limited and protected by business law. Each of the six functional areas of business—management, production and transportation, marketing, research and development, accounting and finance, and human resource management—sits on a foundation of business law.

Law and Its Purposes

LO 1-3 Recall the purposes of law.

Many of us might like to impose rules on others, defining their rights and responsibilities. Few of us can do this as individuals, but a majority of citizens in a democracy can agree to establish rules for business behavior. They can permit certain authorities to make and enforce rules describing what behavior is permitted and encouraged in their community. These rules are what we refer to as the **law**, and they are enforceable in the courts of that community. Exhibit 1-1 lists a few of the numerous purposes fulfilled by the law.

Exhibit 1-1 is a reminder of why we are very proud when we say we are a society of laws. The respect we give to the law as a source of authority is in part a recognition of the fact that in the absence of law, we would rely solely on the goodwill and dependability of one another. Most of us greatly prefer the law to that option.

law

Rules of conduct in any organized society that are enforced by the governing authority of the community.

Classification of the Law

LO 1-4 Distinguish among types of law.

There are many ways of thinking about the law. For example, we can divide law into *national* versus *international* law, *federal* versus *state* law, and *public* versus *private* law. **Private law** involves

private law

Law that involves suits between private individuals or groups.

Exhibit 1-1**Purposes of the Law**

- Providing order such that one can depend on a promise or an expectation of obligations.
- Serving as an alternative to fighting.
- Facilitating a sense that change is possible, but only after a rational consideration of options.
- Encouraging social justice.
- Guaranteeing personal freedoms.
- Serving as a moral guide by indicating minimal expectations of citizens and organizations.

public law

Law that involves suits between private individuals or groups and their government.

civil law

The body of laws that govern the rights and responsibilities either between persons or between persons and their government.

criminal law

The body of laws that involve the rights and responsibilities an individual has with respect to the public as a whole.

disputes between private individuals or groups. As an illustration, if a businessperson owns a computer equipment store and is delinquent in paying rent to the landlord, the dispute between them entails private law. **Public law** involves disputes between private individuals or groups and their government. For instance, if a computer store dumps waste behind its building in violation of local, state, or federal environmental regulations, the resulting dispute focuses on public law.

Another distinction among types of laws is civil law versus criminal law. **Civil law** involves the rights and responsibilities found in relationships between persons and between persons and their government. It also involves the remedies available when someone's rights are violated. For example, in 2009, Mississippi Valley Silica Co. was ordered to pay a plaintiff \$9 million because the court ruled that it sold sand to the plaintiff's employer with the knowledge that using that sand on a regular basis would expose a worker to a form of cancer. Yet, Mississippi Valley did not alert those who bought the sand about the risk.

In contrast to civil law, **criminal law** applies to situations in which someone commits an act against the public as a whole. There are several business activities that can be considered criminal, such as money laundering, bribery, mail fraud, racketeering, price fixing, insurance fraud, embezzlement, and theft of trade secrets. These crimes are prosecuted not by individuals but by the state or federal government.

One example of a criminal law is the prohibition against insider trading on the stock exchange. Insider trading occurs when an individual uses insider, or secret, company information to increase her or his own finances or those of family or friends. For example, several years ago, an IBM secretary allegedly told her husband, who told several other people, that the company was going to take over operations of Lotus Development. This information was spread among a number of individuals before it was publicly announced.

On the basis of this leak, 25 people bought stock that increased greatly in value following IBM's public announcement. The Securities and Exchange Commission filed charges against the 25 stock purchasers because they were creating an unfair trading environment for the public.

Sources of Business Law

LO 1-5 Differentiate between sources of the law.

How is law created, and where do we look to find the laws?

Constitutions

The United States Constitution and the constitution of each state establish the fundamental principles and rules by which the United States and the individual states are governed. The term **constitutional law** refers to the general limits and powers of the federal and state governments as stated in their written constitutions. The U.S. Constitution is the supreme law of the land, meaning that it overrules all federal, state, and local laws that conflict with it and is the foundation for all laws in the United States. It is the primary authority to study when trying to identify the relationship between business organizations and government.

constitutional law

The general limits and powers of a government as interpreted from its written constitution.

Statutes

Legislative actions, called *statutes*, are another important source of law. The assortment of rules and regulations put forth by legislatures is what we call **statutory law**. These legislative acts can be found in the U.S. Code when they are passed by Congress or in the various state codes when they are enacted by state legislatures. The codes are a collection of all the laws in one convenient location.

Because so much business activity occurs within the jurisdiction of state courts, business managers must be familiar with the local city and county ordinances that govern matters not covered by federal or state codes. These ordinances address important business considerations such as local taxes, environmental standards, zoning ordinances, and building codes.

For example, if you want to open a Krispy Kreme franchise in Santa Fe, New Mexico, you must follow local guidelines regarding the area where you may build your store, the materials that you may use to build, and the state minimum wage that you must pay to employees making donuts. The regulations will be different if you want to open your franchise in Toledo, Ohio, or in Seattle, Washington.

Although they are not a source of law in the same sense as constitutions and statutory law, **model** or **uniform laws** serve as a basis for some statutory law at the state level. Business activity is made more difficult when state laws vary. To prevent such problems, a group of legal scholars and lawyers formed the National Conference of Commissioners on Uniform State Laws (NCC). The NCC regularly urges states to enact model laws to provide greater uniformity of law. The response is entirely in the hands of the state legislatures. They can ignore a suggestion or adopt part or all of the proposed model law.

The proposals of the NCC, though not laws themselves, have been adopted on more than 200 occasions by state legislatures. The NCC is an especially important influence on business law. Paired with the publications of the American Law Institute, the NCC became the source of the *Uniform Commercial Code (UCC)*. The UCC is a body of law so significant for business activities that it will be the focus of intensive study in several chapters of this text. The UCC laws include sales laws and other regulations affecting commerce, such as bank deposits and collections, title documents, and warranties. For example, these laws govern the different types of warranties that companies such as Microsoft, Sony, and Honda provide with their products.

Cases

Constitutions, legislatures, and administrative agencies encourage certain behavior and prevent other actions. But the boundaries of these laws are seldom self-explanatory. Consequently, law must be interpreted.

Case law is the collection of legal interpretations made by judges. An alternative name for case law is **common law**. These interpretations are law unless they are revoked later by new statutory law.

Judicial opinions are especially significant for businesses because a modern business often operates in multiple legal jurisdictions. Because statutory laws are subject to interpretation, one court may have interpreted particular laws one way at one business location, and a second court may interpret a similarly worded statute differently at a second business location.

We will often refer to these judicial opinions as “cases.” Be sure to distinguish judicial opinions in your mind from the business cases you may study in your other business classes, where the cases refer to business situations where you are being asked to apply the business principles you have learned.

Courts issue judicial decisions that often include interpretations of statutes and administrative regulations. These decisions contain the reasoning the courts use to arrive at their decisions. The reasoning depends heavily on **precedent**, the use of past decisions to guide future decisions. An earlier decision in a similar fact pattern is a precedent that guides later decisions, thereby providing greater stability and predictability to the law.

The 2014 case of *Air Wisconsin Airlines Corp. v. Hoepfer* (No. 12-315, slip op. Sup. Ct. January 27, 2014) provides an illustration of how important knowledge of business law and precedent can be. Mr. Hoepfer was a pilot for Wisconsin Air. He needed to be certified to fly a new kind of aircraft

statutory law

The assortment of rules and regulations put forth by legislatures.

model laws

Laws created to account for the variability of laws among states. These laws serve to standardize the otherwise different interstate laws. Also called *uniform laws*.

case law

The collection of legal interpretations made by judges. They are considered to be law unless otherwise revoked by a statutory law. Also known as *common law*.

precedent

A tool used by judges to make rulings on cases on the basis of key similarities to previous cases.

his employer bought. At the conclusion of his fourth failed attempt to be certified, Mr. Hoyer raised his voice, tossed his headset, used profanity, and accused the instructor of railroading him.

The manager who booked a return flight for Hoyer discussed Hoyer's behavior with officials of Wisconsin Air. They knew that Hoyer was licensed to carry a firearm. Consequently, an airline executive warned the Transportation Security Administration (TSA). During the call, the executive said that the airline was concerned about Hoyer's mental stability and the whereabouts of his firearm.

The TSA removed the pilot from the airplane, searched him, and questioned him about the whereabouts of his firearm. Hoyer sued for defamation. The jury found for Hoyer, and the Colorado Supreme Court agreed with the jury on appeal.

When the U.S. Supreme Court heard the case, it reversed the decision, finding against Hoyer's defamation claim. In the course of that opinion, Justice Sotomayor, writing for the Court, relied heavily on the earlier *Masson v. New Yorker Magazine, Inc.*, 501 U.S. 496 (1991) case for precedent.

Hoyer maintained that the Wisconsin Air executive who warned the TSA should have qualified the concern about the location of Hoyer's weapon by saying that "it had no reason to think he actually was armed." But Justice Sotomayor pointed out that *Masson* provided that in a defamation action a materially false statement would have to be one that would have had a different effect on the mind of the listener from that which the truth would have produced and, in this case, a reasonable TSA officer would have searched the pilot for a gun after hearing that the pilot was upset.

It is crucial for business managers to pay attention to changes in the law and cases in which new precedents are set. These precedents must be taken into account when making future business decisions. For instance, courts sometimes make new rulings regarding the kinds of warnings companies should be required to provide to consumers about potential harm that could result from their products.

One example was a case filed against McDonald's. After a woman was severely burned by very hot coffee, the company was found negligent for failing to provide a warning label on its hot-beverage cups. Now many retailers of hot beverages provide warning labels on their beverage cups because of the precedent that was set by this case.

When courts rely on precedent, they are obeying **stare decisis** ("standing by the decision"). Following stare decisis creates greater predictability for both businesses and individuals that look to the courts for the rules on which they should rely when they engage in market exchanges. In accordance with stare decisis, rulings that are made in higher courts become binding precedent for lower courts.

Even though this practice is meant to create a consistent and reliable justice system, different judges may view the facts of a case in different ways. In addition, courts are sometimes presented with a new issue and do not have a binding decision to follow. In such instances, they may look to decisions made in similar cases by nonbinding courts in other states or jurisdictions.

If a new issue comes before two state courts and there is no binding decision from the state supreme court, both state courts need to look for other rulings on similar cases. They are not bound by each other's decision, so they might have different decisions on the same subject. The decisions in these lower courts can be appealed to the state appeals court, however, and the appeals court's decision can be appealed to the state supreme court.

One example of a case that has been used in accordance with stare decisis as a binding precedent is *Brown v. Board of Education*,¹ which abolished discriminatory policies for individuals of different racial backgrounds. For instance, in *Regents of the University of California v. Bakke*,² the plaintiff, a white male, had applied to the University of California at Davis medical school two years in a row and been denied admittance. He alleged that the admissions process was discriminatory because out of 100 slots, 16 were reserved for members of minority races.

The U.S. Supreme Court found that the school's admissions policy was not legal, referencing *Brown* and stating that the basic principle behind it and similar cases was that individuals could not be excluded on the basis of race or ethnicity. The Court wrote, "Preferring members of any one group for no reason other than race or ethnic origin is discrimination for its own sake."

stare decisis

"Standing by the decision"; a principle stating that rulings made in higher courts are binding precedent for lower courts.

¹ 347 U.S. 483 (1954).

² 438 U.S. 265 (1978).

Just as state statutes have been strongly influenced by the suggestions of the NCC, common law evolves with the assistance of a mechanism called **Restatements of the Law**. These Restatements are summaries of the common law rules in a particular area of the law that have been enacted by most states.

In addition to the Restatements, many influences are at work in the minds of judges when they interpret constitutions, statutes, and regulations. For example, the values and social backgrounds of the judges function as lights and shadows, moving the judges toward particular legal decisions.

Administrative Law

Constitutions and statutes are never complete in the sense of covering all the detailed rules that affect government and business relations. The federal government, as well as state and local governments, has dozens of administrative agencies whose task is to perform a particular government function. For example, the Environmental Protection Agency (EPA) has broad responsibilities to enforce federal statutes in the area of environmental protection.

Administrative law is the collection of rules and decisions made by all these administrative agencies. Just glance at Exhibit 1-2 to get a sense of the scope of a few of the major federal administrative agencies.

Businesses function within the rules established by agencies like these. For example, the Occupational Safety and Health Administration (OSHA) oversees health and workplace safety and makes sure that employees are working in conditions that are not hazardous.

In 2015, illustrating the implications of OSHA for business managers, Walmart was fined \$7,000 when a store in Valley Stream, New York, did not “furnish a place of employment which was free from recognized hazards that were causing or likely to cause death or serious physical harm to employees in that employees were exposed to the hazards of asphyxiation or being struck due to crowd crush, crowd surge or crowd trampling.” Walmart’s managers and employees failed to provide effective crowd management training and did not use appropriate crowd management techniques to safely manage a large crowd of approximately 2,000 customers.

Treaties

A *treaty* is a binding agreement between two states or international organizations. Treaties may be called several things: international agreements, covenants, exchanges of letters, conventions, or protocols. In the United States, a treaty is generally negotiated by the executive branch. To be binding, it must then be approved by two-thirds of the Senate.

A treaty is similar to a contract in two important ways. Both treaties and contracts are attempts by parties to determine rights and obligations among themselves. In addition, when a party fails to obey a treaty or an international contract, international law imposes liability on that party.

Restatements of the Law

Summaries of common law rules in a particular area of the law. Restatements do not carry the weight of law but can be used to guide interpretations of particular cases.

administrative law

The collection of rules and decisions made by administrative agencies to fill in particular details missing from constitutions and statutes.

INDEPENDENT AGENCIES	EXECUTIVE AGENCIES
Commodity Futures Trading Commission (CFTC)	Federal Deposit Insurance Corporation (FDIC)
Consumer Product Safety Commission (CPSC)	Occupational Safety and Health Administration (OSHA)
Equal Employment Opportunity Commission (EEOC)	General Services Administration (GSA)
Federal Trade Commission (FTC)	National Aeronautics and Space Administration (NASA)
Federal Communications Commission (FCC)	Small Business Administration (SBA)
Interstate Commerce Commission (ICC)	International Development Cooperative Agency (IDCA)
National Labor Relations Board (NLRB)	National Science Foundation (NSF)
National Transportation Safety Board (NTSB)	Veterans Administration (VA)
Nuclear Regulatory Commission (NRC)	Office of Personnel Management (OPM)
Securities and Exchange Commission (SEC)	

Exhibit 1-2

Major Federal Administrative Agencies

Executive Orders

The president and state governors can issue directives requiring officials in the executive branch to perform their functions in a particular manner. The Code of Federal Regulations (CFR) contains all the executive orders created by the president. (The CFR is online at <https://www.govinfo.gov/help/cfr/>.) Presidents claim the power to issue such orders on the basis of their Article II, Section 1, constitutional power to “take care that the laws be faithfully executed.”

President Biden issued 28 executive orders during his first three weeks, making him the president who has issued the most executive orders ever in that initial period of a presidency. His level of activity is a continuation of a trend toward Executive Branch assertiveness amidst a general sense that legislatures move too slowly to address immediate problems.

An illustration of an especially controversial executive order is Order 9066, issued by President Franklin Roosevelt during World War II. On the basis of this order, Japanese-Americans on the West Coast, as well as thousands of Italian-American and German-American families, were sent to internment camps for the duration of the war.

Schools of Legal Interpretation

LO 1-6 Identify the various schools of jurisprudence.

When legislators or courts make law, they do so guided by certain habits of mind and specific beliefs about human nature. These views guide them toward particular legal solutions and away from others. This section briefly describes several of the more common guides to legal interpretation.

The point of learning about these alternative methods for interpreting the implications of particular legal facts is to encourage you to see the law as a human creation shaped by many perspectives and approaches to what a court decision or statute means. That there are multiple interpretations of a statute or a set of facts does not mean that all are equally thoughtful or directly relevant. Instead, considering alternative perspectives serves to broaden the necessary narrowness of the perceptions of individuals.

identification with the vulnerable

A school of jurisprudence that holds that society should be fair. Particular attention is therefore paid to the poor, the ill, and the elderly.

Identification with the Vulnerable Some thoughtful legal scholars claim that our very nature as humans compels us to advance the law on the basis of **identification with the vulnerable**. Some members of our society can take care of themselves in terms of most life situations. Others, especially the ill, children, the aged, the disabled, and the poor, require assistance to meet their fundamental needs of life, health, and education.

This guide to legal change is tied closely to the pursuit of fairness in our society. The metaphor of a level playing field is linked with some higher law or body of moral principles that connects all of us in the human community. We might look at a particular employment contract, for example, and react by observing that “it is just not fair.” Our caring impulse as a human feels outrage at that legal arrangement. That outrage can be a stimulus for legal change. One example of identification with the vulnerable is minimum-wage laws. They reflect the beliefs that workers should receive a minimum hourly wage and that employers should not be allowed to pay them less.

historical school

A school of jurisprudence that uses traditions as the model for future laws and behavior. Also called *tradition* or *custom*.

Historical School: Tradition One of the most often used guidelines for shaping the law is **tradition**, or *custom*, which is also called the **historical school**. *Stare decisis* is rooted in this perspective. When we follow tradition, we attempt to link our future behavior to the behavior of those who faced similar problems in earlier historical periods. The logic of the approach is that we need not reinvent the wheel each time a legal problem arises. Past practice is assumed to have been the product of careful thought.

Originalism

The interpretation of legal texts such as the Constitution by relying on the words or intent of the creators of the text in question.

Originalism is a theory of interpretation of legal texts—particularly the Constitution—that believes that these texts should be interpreted according to their “original meanings.” Some originalists argue that a text should be interpreted according to the intentions of its authors (e.g., the Constitutional Framers). Others hold that the words of a legal text should be read with their “original public meaning,” or the meaning the public gave to the words at the time of writing.

Although there are various shades of originalism, a core goal shared by most originalists is to read legal texts in an objective way without imposing our own modern interpretations of them.

Originalists use a variety of resources to try to determine the original meaning or intent of a legal text. An originalist might use a dictionary, grammar book, or similar legal document from the time to determine how a particular word was used by lawyers, legislators, or the public. Originalists hope that by using the original meaning of the words of a legal text or the original intent of its authors, our law will be applied more objectively and fairly.

Legal Realism **Legal realism** is based on the idea that, when ruling on a case, judges need to consider more than just the law. This school of thought dictates that they also take factors such as social and economic conditions into consideration when making a judgment. Followers of legal realism argue that the law must not be the sole factor in deciding a case since legal guidelines were designed by humans and exist in an ever-changing society.

Judges who follow this school of thought are more likely to depart from past court decisions to account for the fact that our society is constantly shifting and evolving. Those who subscribe to legal realism also believe that the law can never be enforced with complete consistency. They argue that because judges are human, they will bring different methods of reasoning to very similar cases.

One example of a law that has been enacted to reflect changes in our society is the Family and Medical Leave Act (FMLA). This act mandates that businesses employing more than 50 people must provide their workers with up to 12 weeks' unpaid leave every year to take care of family-related affairs such as caring for ill parents, adopting a child, or having a child. The FMLA protects pregnant women who take time off work because their employers must provide them with the same pay and the same or an equivalent job when they return to work. This act reflects the fact that more mothers are working outside the home and more women are returning to work soon after they have a child. The FMLA also protects new parents against some types of employer discrimination that might occur after they return to work.

Cost-Benefit Analysis From this perspective, we need to examine all the costs and benefits for alternative laws or decisions and place monetary values on those costs and benefits. If we possessed those calculations, we could use **cost-benefit analysis** as a guide to legal change, choosing the legal alternatives that maximize the ratio of benefits to costs. For instance, in a contract dispute, someone using this approach would attempt to attach responsibility for the problem in such a way that total benefit is maximized in relation to costs.

This approach to legal change is tied closely to the pursuit of efficiency. If a law yields more benefits than costs, then we have saved resources. Those resources can, in turn, be used to provide us with more goods and services. Our economy is thus more efficient in the sense of producing more for less.

For example, regulations enacted by the EPA can affect costs and benefits in the national economy. Polluted land is an economic loss because it cannot be used for farming or recreation. Polluted water can be toxic for fish and cannot be used for drinking. Polluted air can cause health problems and result in higher health care costs. Although EPA regulations may end up costing companies more initially to control pollutants, the cost of environmental cleanup, and the loss of productivity in the economy as a whole, may be greater than the resources companies expend to control pollution.

legal realism

A school of jurisprudence that holds that context must be considered as well as law. Context includes factors such as economic conditions and social conditions.

cost-benefit analysis

An economic school of jurisprudence in which all costs and benefits of a law are given monetary values. Laws with the highest ratios of benefits to costs are then preferable to those with lower ratios.

Global and Comparative Law

Comparative and international law is extremely important for future business managers. Because of advances in technology and transportation, trade with other countries is far easier today than it was in past years. Now it is possible to make different components for the same product in various countries all over the world and then assemble them in another country. It is possible to operate an antique store in Poughkeepsie but sell to customers in Moscow or Taipei through a website.

As a result of this ease in trade, business managers must be familiar with global trade laws that regulate business practices among nations. For instance, the United States and other countries have entered into agreements such as the North American Free Trade Agreement (NAFTA) and the General Agreement on Tariffs and Trade (GATT). These agreements help establish the conditions of trade between countries.

In 1995, the World Trade Organization (WTO) was created to replace GATT. The WTO stimulates negotiations among member nations to reduce barriers to international trade. The WTO attempts to enforce trade agreements governing trade among its 160 member nations.

In this role, it serves as a world court adjudicating trade disagreements that threaten to disrupt international trade.

It is also important for future business managers to understand comparative law, comparing and studying the laws in different countries. Business managers need to be aware of various trade laws and restrictions in different countries so that they can act accordingly when they set out to do business in those countries. The European Union, for example, has laws that differ from those of the United States in terms of regulating the taxes on Internet sales and the amount of pollution that can be released into the environment. Companies doing business in the EU must take these standards into account.

For example, contrast the extent that the Chinese and American governments explicitly gather data on their citizens. The Chinese government does not want its citizens to have access to certain information and websites. A Chinese cybersecurity law that went into effect in June 2017 requires firms that do business in China to store in China all data that firms have on Chinese citizens and businesses. The law includes further strict guidelines, including ensuring that the data contains no “state secrets prior to transferring the data outside the country” (though the Chinese government decides what information is considered a “state secret”). The law also requires any “critical network equipment” and “specialized cybersecurity products” to be approved by the Chinese government before they can be sold in China (likely included to ensure that the products cannot bypass China’s internet restrictions). One of the impacts of the 2017 law was the creation in 2021 of the Personal Information Protection Law that governs the processing of personal information of individuals located in China, regardless of whether the entities processing that information are in China.

As an additional illustration of the importance of being aware of the diversity of law in different countries, just imagine the problems that could arise if you were to need space for your business in Vietnam, but the only property law you knew was U.S. property law.

In the United States, we take for granted the right to purchase a piece of property if we have the money to do so. Property is not so freely available and transferable in all nations. Vietnam’s new constitution, written in 1992, provides guidelines for the allocation, transfer, and sale of private property. However, it still asserts that the people, or the state, own all the land.

Thus, if individuals or private enterprises want to use land, they must pay tax on it as a form of rent and are granted a “use of right” that entitles them to extended use and the freedom to transfer the property. Technically, they are transferring not the *property* but, rather, the right to use it. Transference of property rights can occur only with the approval of a state official. The official ensures that the new owner intends to use the land for the original, state-approved purpose.

Moreover, the new owner can never be given a longer term of right or more extensive rights over the land than the original owner had. Finally, the state official determines the price that the property will be transferred for. The government has specified certain prices depending on how the land is used.

Modern business managers must have an ongoing fascination with the law to function effectively. Business law tells business managers the basic rules of the business game. Play any game without having first studied the rules, and you will probably fail.

But, unlike an ordinary game, the business game has a rule book that is changing dynamically. In addition, increased globalization requires business leaders to be alert to legal differences among national jurisdictions.

PRACTICAL TIPS for Business Managers

1. Remember that the meaning and implications of laws are a matter of interpretation. Therefore, it is wise, if possible, to consult with more than one lawyer when you are curious about the meaning of a law that is immensely important to your operations.
2. Try to stay current with your knowledge of law relevant to your industry and that of your suppliers. Law evolves, and yesterday’s law may not be today’s law.
3. When you engage in any international commercial activity, be sure to investigate the law of countries in which you are doing business.

Questions & Problems

1. What is the difference between private law and public law?
2. What are the main distinctions between the different schools of legal interpretation?
3. If there are different ways to interpret statutes and case decisions, would it make sense to say that all interpretations of the law are equally appropriate?
4. Presidential elections are partially about who will be able to select Supreme Court judges. As you look at the various alternative ways to interpret and apply the law, which of those methods of interpretation would you hope is held by your favorite candidate for president?
5. Most business managers know they need to consult a lawyer when they make important business decisions. If that assumption is correct, why would managers or entrepreneurs need to have any knowledge of business law? Couldn't they just ask the lawyer?
6. Appendix 1A provides guidance for becoming a better critical thinker. A recent *Forbes* poll of business leaders found that the most important skill business leaders are seeking in their employees is critical thinking. As you study the appendix, why do you think this skill of critical thinking is so valuable to business managers?
7. This chapter distinguishes between private and public law. Why are the interests of the public identified with the behavior of the government? Why would public law not be a term referring to the interests of corporations, for example?
8. What is the need for a special area of law for administrative agencies? Why would the law as it applies to businesses not apply just as well to administrative agencies?
9. Choose an area of law that fascinates you. Spend some time on the Internet searching for differences between how the United States and other countries respond to conflicts among people within that area of law, just as we did in the text in the illustration of real property law in Vietnam.
10. Jarold Daniel Friedman worked as a temporary computer contractor for a pharmaceutical warehouse. The warehouse offered him a permanent position, but the warehouse required him to get a mumps vaccine, grown in chicken embryos, as a condition of his permanent employment. Friedman, a vegan, believed that the vaccination would violate his religious beliefs and declined to be vaccinated. As a result, the warehouse withdrew its offer of employment. Friedman claimed that the warehouse discriminated against him on the basis of religion. Do you agree with Friedman? Do employers have a duty to respect the beliefs of their employees? If so, what happens when that duty conflicts with employers' duty to provide a safe and healthy work environment?

Source: *Friedman v. Southern California Permanente Medical Group*, 102 Cal. App. 4th 39 (2002).

APPENDIX 1A

Critical Thinking and Business Law

Success in the modern business firm requires the development of **critical-thinking skills**—the ability to understand what someone is saying and then to apply a set of evaluative criteria to determine the worth of what was said. In other words, businesspeople need to be able to sort sense from nonsense by evaluating arguments about relevant business law.

A critical thinker is always asking, “Now does that make sense?” And there is no better context in which to develop critical-thinking skills than in the study of the laws that affect business. Critical-thinking skills learned in the study of business law will be easily transferred to the decisions of business stakeholders.

Legal reasoning is similar to other reasoning in some ways and different in others. When people, including lawyers and judges, reason, they do so for a purpose. Some problem or dilemma bothers them. The stimulus that gets them thinking is a *legal issue*. It is stated as a question because it is a call for action. It requires us to *do* something, to think about answers.

For instance, we may be interested in such issues as the following:

- When are union organizers permitted under the National Labor Relations Act to trespass on an employer's property?
- Do tobacco manufacturers have liability for the deaths of smokers?
- Must a business fulfill a contract when the contract is made with an unlicensed contractor in a state requiring all contractors to be licensed?

critical-thinking skills

The ability to understand the structure and worth of an argument by evaluating the facts, issue, reasons, and conclusion of that argument.

Each of these questions has several potential answers. Which answer best accomplishes a particular business objective? Which answers are consistent with the law? Here is where critical thinking is essential to business success. Some answers can get the decision maker into trouble; others will advance the intended purpose. Each answer is called a *conclusion*.

Business firms often come into contact with such conclusions in the form of laws or court decisions. Business managers are therefore both consumers of and contributors to these legal conclusions. As businesspeople learn about and react to decisions or conclusions made by courts, they have two primary methods of response:

1. Memorizing and understanding the conclusions or rules of law as a guide for future business decisions.
2. Making judgments about the quality of the conclusions.

This book encourages you to do both. There are many forms of critical thinking, but they all share one characteristic: they focus on the quality of someone's reasoning. Critical thinking is active; it challenges each of us to form judgments about the quality of the link between a set of reasons and the conclusion supposedly derived from them. In particular, we will be focusing on the link between a court's reasons and its conclusions.

Our reactions to legal arguments shape our efforts either to support the status quo in the legal environment of business or offer support for particular changes.

The following structure for critical thinking is a thoroughly tested method that successful market decision makers use. Every time you read a case, try to follow this pattern of careful thinking:

1. Find the facts.

Facts: Here, we are looking for the most basic building blocks in a legal decision or argument. These building blocks, or facts, provide the environment or context in which the legal issue is to be resolved. Certain events occurred, certain actions were or were not taken, and particular persons behaved or failed to behave in specific ways. All of these and many more possibilities together make up the intricate setting for the playing out of the issue in question. We always wonder, "What happened in this case?" A major feature of this book is called "But What If." This feature highlights the importance of facts in legal reasoning by focusing attention on the huge effect of changes in single facts on success or failure in a legal dispute.

2. Look for the issue.

Issue: In almost any legal conflict, finding and expressing the issue is an important step in forming our reaction. The issue is the question that caused the lawyers and their clients to enter the legal system. Usually, there are several reasonable perspectives concerning the correct way to word the issue in dispute. Don't let the possibility of *multiple* useful ways to word the issue cause you any confusion. The legal issue is certainly not just anything that we say it is.

3. Identify the judge's reasons and conclusion.

Reasons and conclusion: Judges do not form legal conclusions on the basis of whim. They have support for their decisions. That support consists of their reasons. When we ask someone *why* a judge formed a particular conclusion, we are showing our respect for reasons as the proper basis for any assertion. We want a world rich with opinions so that we can have a broad field of choice. But we should agree with only those legal opinions that have convincing reasons supporting the conclusion. Asking "Why?" is our way of saying, "I want to believe you, but you have an obligation to help me by sharing the reasons for your conclusion."

4. Locate in the decision the rules of law that govern the judge's reasoning.

Rules of law: Judges cannot offer just any reasoning that they please. They must always look back over their shoulders at the laws and previous court decisions that together provide an anchor for current and future decisions. What makes legal reasoning so complex is that statutes and legal findings are never *crystal* clear. They may seem very clear, but judges and businesspeople have room for interpretive flexibility in their reasoning.

5. Apply critical thinking to the reasoning.

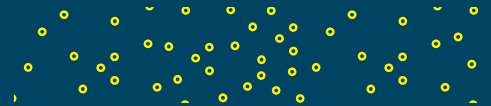
Evaluation of the reasoning: A judge's reasoning, once it has been laid before us by following the steps discussed here, is a message that we may either accept or reject. One of the most exciting things about our legal system is its potential for change. **Critical thinking in the legal context** consists of examining the legal opinion in search of potential problems in the reasoning.

Here is a small sample of some especially useful critical-thinking guidelines for business managers to apply when thinking about business law:

- *Look for potential ambiguity in the reasoning.* The term *ambiguity* refers to a lack of clarity in a word or phrase in the reasoning. Many words have multiple meanings; until the intended meaning is discovered, we cannot tell whether we want to agree or disagree with the reasoning.
- *Ask whether the analogies used in the decision are strong.* When judges follow particular precedents, they are saying that the key similarities between the facts in the precedent and those in the case at hand are so similar that it makes sense to apply the same rule of law in both. Are there key differences in the factual situations that raise questions about the quality of that analogy?
- *Check the quality of the judge's use of evidence in his or her reasoning.* Is the evidence used by the judge to support the opinion both abundant enough and reliable enough that we should agree with the reasoning?
- *Think about the extent to which important missing information prevents you from being totally confident about the judge's reasoning.* Is there important missing information that you would need to have before making up your mind?
- *Consider the possibility of rival causes.* When the judge claims that one action caused another, think about whether some alternative cause may have been responsible.

critical thinking in the legal context

Examining a legal opinion to search for potential problems in the reasoning.



Part 1 *The Legal Environment of Business*

CHAPTER 2

Business Ethics and Social Responsibility

LEARNING OBJECTIVES

- LO 2-1** Distinguish between business ethics and the social responsibility of business.
- LO 2-2** Recognize the relationship between business law and business ethics.
- LO 2-3** Define values.
- LO 2-4** Explain how values provide a starting point for thinking about business ethics.
- LO 2-5** Analyze business decisions using the WH framework.

LO 2-1 Distinguish between business ethics and the social responsibility of business.

What business managers should do when their decisions have impacts on a wide assortment of stakeholders is not altogether clear. Ethical conversation is less about finding the one and only right thing to do than it is about finding the better thing to do. Whatever you choose to do, some stakeholders will be hurt and others will benefit. Business ethics requires a thought process that weighs the benefits of a decision compared to its harm, consideration of the duties we owe other human beings, the characteristics possessed by a virtuous person, and the care we have for the well-being of those affected by business decisions.

Understanding what business ethics is and is not expands our appreciation for the difficulties involved when a firm is trying to earn a large profit and at the same time genuinely attempting to be a reliable corporate citizen. The temptation to treat customers as an instrument for the enrichment of the business can be seductive. Resisting that temptation requires business leadership that treats customers, employees, and the community with the same respect naturally assigned to owners of the firm.

One useful distinction identifying the boundaries of ethics is that between ethics and morals. The latter consists of the performance expectations a culture has at any time for business behavior. For example, some cultures see bribes as an ordinary and acceptable lubricant for transactions. The morality of a firm in such a culture includes the assumption that bribes will be a normal occurrence as part of ordinary business interactions.

Ethics is a more complicated set of expectations because it refers to reflection about what morals *should be*. In the illustration above, ethics would involve a conversation about and determination of optimal firm behavior. Who is harmed by those bribes? What is the effect on future generations of a morality tolerant of bribes? To what extent do bribes limit business opportunities in that the capability to pay bribes resides overwhelmingly in the hands of those who have already been financially successful?

To think about the ethics of a decision requires us to have a language that accelerates consideration of what is good and right. A central objective of this chapter is to make you aware of the ideas and words we use when we tackle an ethical dilemma.

This chapter provides some assistance for thinking systematically about issues of right and wrong in business conduct. Initially, we need to sort through the meaning of key terms like *business ethics* and *social responsibility*. Then, because it is helpful to have a useful approach to ethical decision making, we provide a practical method by which future business managers can think more carefully about the ethical dilemmas they will face during their careers.

A business has a huge assortment of responsibilities. Each responsibility involves a relationship with other people in the community. Some of the responsibilities are more obvious than others. Firms have a responsibility to devote their energies to fulfilling the interests of their owners, certainly. The pursuit of profits is both a stimulus for incredible innovation and efficiency and a temptation to use whatever power the firm has to conceal information from consumers and the public.

In addition, business firms owe safe working conditions to the employees who make it possible for the firm to thrive. Increasing the safety of the workplace can diminish profits, at least in the short run. Business ethics is full of dilemmas such as the extent to which short-term profits can be achieved at the cost of reduced safety for employees.

Other responsibilities are just as real but perhaps less obvious. A business firm must obey the laws in the countries where it offers its products and services. This course spells out many of those responsibilities, and the list is quite extensive. In addition, firms have a much more abstract ethical responsibility to obey the standards of conduct consistent with prevailing ethics and expectations in the communities where they practice their trade.

Ethics is the study and practice of decisions about what is good or right. Ethics guides us when we are wondering what we should be doing in a particular situation. **Business ethics** is the application of ethics to the special problems and opportunities businesspeople experience. An **ethical dilemma** is a problem about what a firm should do, for which no clear, right decision is available. Reasonable people can expect to disagree about optimal solutions to ethical dilemmas.

ethics

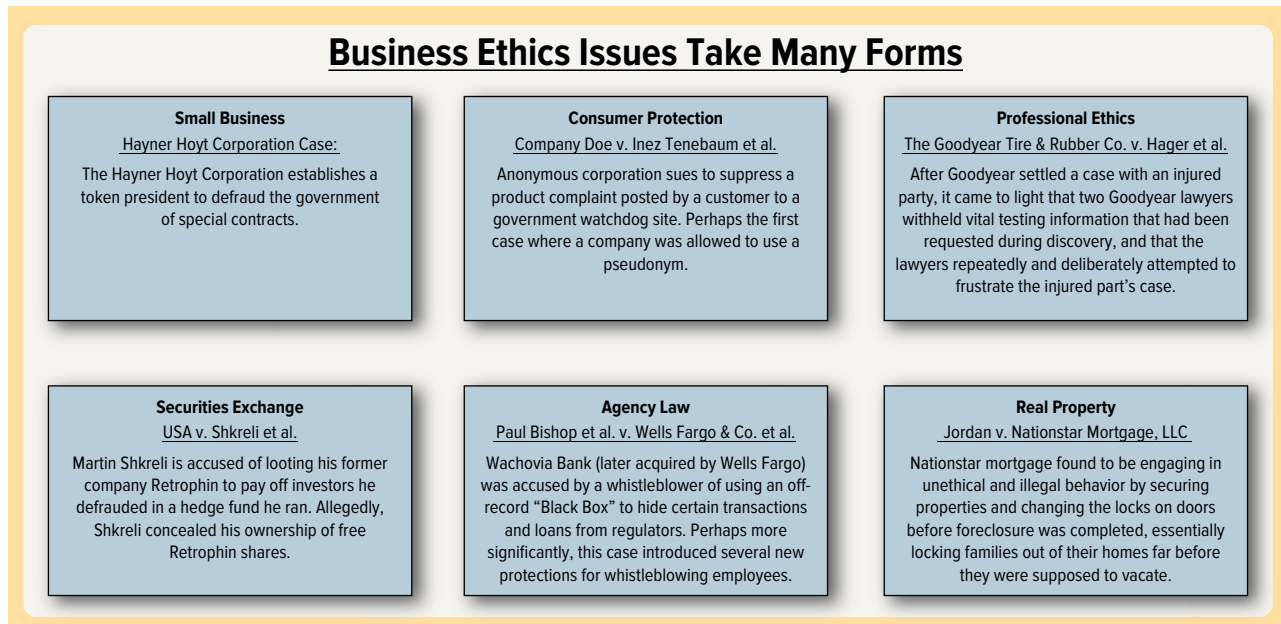
The study and practice of decisions about what is good or right.

business ethics

The use of ethics and ethical principles to solve business dilemmas.

ethical dilemma

A question about how one should behave that requires one to reflect on the advantages and disadvantages of the optional choices for various stakeholders.

Exhibit 2-1 Business Ethics Issues Take Many Forms**social responsibility of business**

The expectations that a community places on the actions of firms inside that community's borders.

Closely related to ethical dilemmas arising in business situations is the concept of the social responsibility of a business. The **social responsibility of business** consists of the expectations the community imposes on firms doing business within its borders. These moral expectations must be honored to a certain extent, even when a firm wishes to ignore them, because firms are always subject to the implicit threat that legislation will impose social obligations on them. So, if the community expects businesses to obey certain standards of fairness even when the standards interfere with profit maximization, firms that choose to ignore this expectation do so at their peril.

The analogy here is to the role of a good citizen. The community guarantees you certain protections and rights. In return for that support network, we owe responsibilities of civic engagement and obedience to the law. A business firm gets the protection of laws designed to provide stability and productivity in their activities. Its social responsibilities extend to the expectations the community has for how a business should behave.

The definition of business ethics refers to *standards* of business conduct. *It does not result in a set of correct decisions.* Business ethics can improve business decisions by serving as a reminder not to simply choose the first business option that comes to mind or the one that enriches the firm in the short run. But business ethics can never produce a list of correct business decisions that all ethical businesses will make.

Exhibit 2-1 provides a picture of the broad scope of business ethics. Many decisions made by managers and entrepreneurs affect a huge array of people inside and outside the walls of the business. Those effects raise issues of what is right, fair, and acceptable. Consequently, business ethics is an essential part of business planning and strategy.

Business Law and Business Ethics

LO 2-2 Recognize the relationship between business law and business ethics.

Before business managers consider the social responsibilities of firms in their communities, they need to gather all the relevant facts. Experienced managers know that assembling the facts is just the beginning of a thoughtful business decision. Next, it makes sense to ask, *Is it legal to go forward with this decision?*

The legality of the decision is the minimal standard that must be met. But the existence of that minimum standard is essential for the development of business ethics. Think of the law as the most recent consensus about the lower level of business ethics. We can expect that minimum to

BUSINESS Ethics Flashpoint 2.1

Chevron in Ecuador

In 1964, Texaco Petroleum (now known as Chevron), along with Gulf Oil Corporation (Gulf), was invited by the Ecuadoran government to conduct exploratory activities in the eastern region of Ecuador. This region was known as the Oriente.

In 1967, Texaco and Gulf discovered large quantities of oil in the Oriente. After building a pipeline that would allow for the transfer of oil to the Pacific coast, Texaco began exporting the oil.

Texaco acted as the operator in a partnership, known as a consortium, between Texaco and Gulf. In 1973, production reached 200,000 barrels of oil per day. During this period, Ecuador's gross national product (GNP) had doubled.

During the early 1970s, the military seized control of the Ecuadoran government. This takeover resulted in a series of governmental reforms that limited the size of concession areas granted to foreign oil companies such as Texaco. Texaco, therefore, relinquished some of its concessions to Ecuador's state-run oil company, Petroecuador. In addition, Petroecuador joined the consortium between Texaco and Gulf.

Soon after Petroecuador joined the consortium, Gulf left. The consortium, now consisting of only Texaco and Petroecuador, lasted from 1977 until 1990. In 1992, Ecuador did not renew Texaco's concessions. As a consequence, Texaco's interest in the oil industry came to an end.

During the period in which it operated in Ecuador, Texaco's oil-related operations exacted a great toll on the residents of the Oriente.

For example, Texaco dumped billions of gallons of toxic wastewater into surrounding rivers and streams of the Amazon. Texaco is also reported to have spilled about 17 million gallons of crude oil into surrounding lands in the Oriente. Another source reports that about 2.5 million acres of land were affected by the leaking of oil into soil and groundwater, as well as by oil discharges into wetlands, streams, and rivers. In addition, Texaco had allegedly stored toxic chemicals in hundreds of unlined pits. The waters that indigenous groups relied on for drinking, cooking, bathing, and fishing became receptacles for Texaco's garbage.

Another source of environmental damage in the Oriente region was gas flaring and the burning of crude oil. These acts resulted in toxic fumes that polluted the air.

The contaminated water and polluted air in the region of the Oriente had significant effects on the health of the residents living in the Oriente. A little more than 8,000

residents suffered one or more diseases attributable to the contaminants with which Texaco polluted the area. The people of the Oriente reported higher rates of cancer than the general population of Ecuador and in other Amazonian provinces. Birth defects were also attributed to the environmental pollution. However, despite these adverse effects on the surrounding population, Texaco did not endeavor to address these problems during its operations.

In addition to suffering from diseases related to toxic contaminants, the indigenous population in the Oriente suffered economic losses. For example, 75 percent of Oriente residents reported that they had suffered from loss of their crops as well as loss of animals on which they relied because of Texaco's toxic discharges into the environment. Texaco's clearing substantial parts of natural habitat to make room for oil operations also contributed to the elimination of the region's forests. Thus, the contamination of the natural habitat in the Oriente led not only to disease but also to economic and cultural losses.

In 1993, 46 residents of Ecuador who belonged to numerous indigenous tribes in the Oriente filed a suit against Texaco (now known as Chevron due to a merger) seeking redress for Texaco's actions. Texaco denied allegations of a causal connection between its oil operations and the diseases reported.

Additionally, Chevron endeavored to exclude Ecuador from trade negotiations with the United States until Ecuador shut down the lawsuit. To this action, then-Senators Barack Obama and Patrick Leahy responded: "While we are not prejudging the outcome of the case, we do believe the 30,000 indigenous residents of Ecuador deserve their day in court . . ."

After numerous proceedings that began in New York and then moved to Ecuador, the plaintiffs were awarded \$19 billion in damages—later reduced to \$9.5 billion—in February 2011, for purposes of restoring the environment, providing health care treatment, and obtaining clean water. However, Chevron refused to pay this fine.

On March 4, 2014, a U.S. federal judge blocked U.S. courts from being used to collect the \$9.5 billion judgment against Chevron. The U.S. court concluded that the Ecuadoran courts had been influenced by corrupt relations between judges and attorneys representing the indigenous groups. As a consequence, Chevron's fine was essentially revoked.

Sources: Trudie Styler, "Seeking Justice in Ecuador," March 5, 2014, HuffingtonPost.com; Lucien J. Dhooze, *Aguinda v. ChevronTexaco: Mandatory Grounds for the Non-Recognition of Foreign Judgments for Environmental Injury in the United States*, 19 J. of Transnational Law & Policy 1 (2009).

evolve alongside new technologies, emerging demographic patterns, and continuing growth in our empathy for marginalized voices in our country.

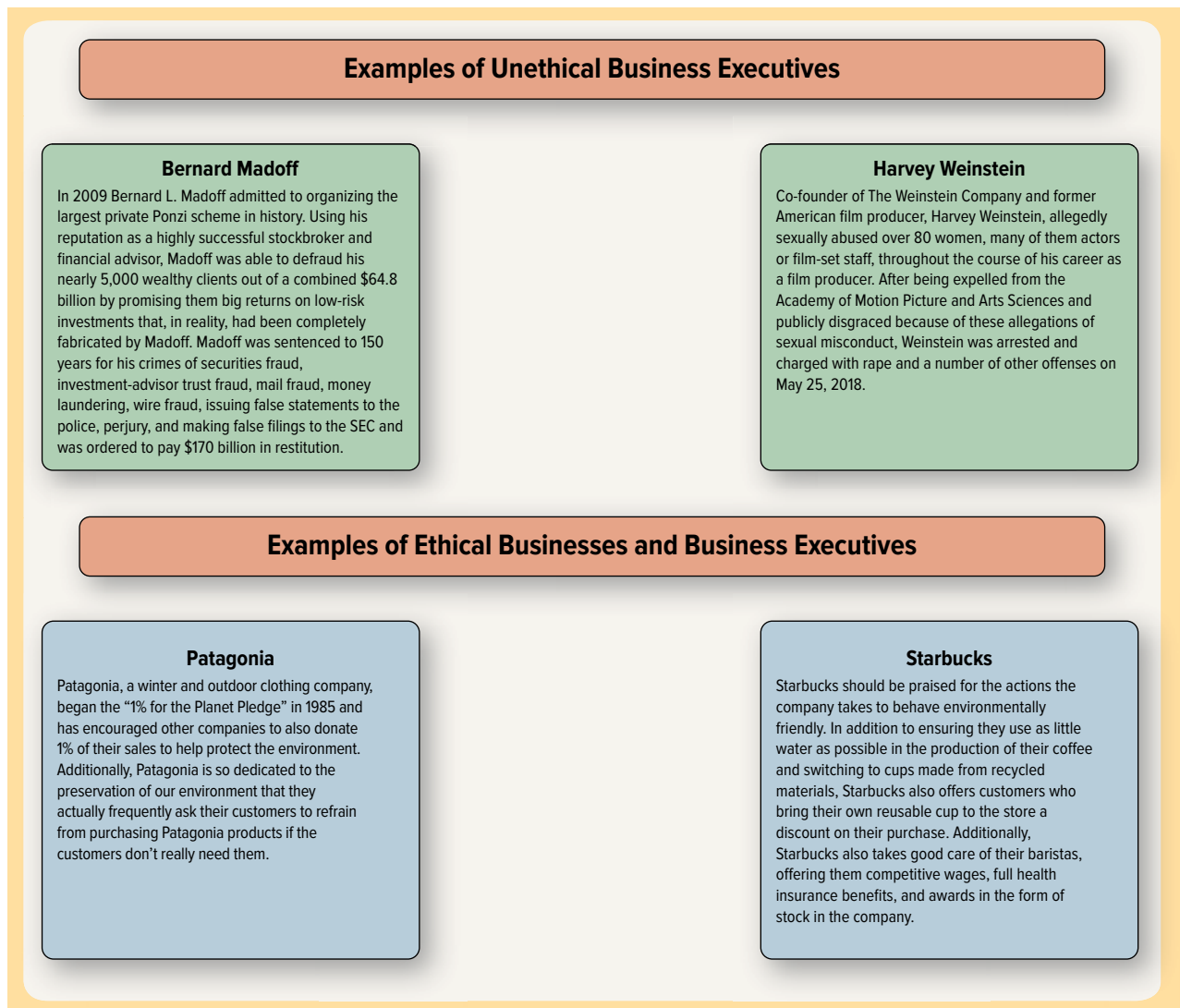
To make this point, let's take a look at the growing practice of bribery in the absence of legal standards. In some countries, businesses must pay bribes to receive legitimate supplies. Although the businessperson may be morally opposed to paying the bribes, the supplies are necessary to stay in business, and there may be no other means of obtaining them.

Thus, foreign companies face an ethical dilemma: they must decide whether to pay bribes or find alternative sources of supplies. For instance, when McDonald's opened its doors in Moscow, it made arrangements to receive its supplies from foreign providers. These arrangements ensured that the franchise did not have to engage in questionable business practices.

At the same time that business ethics guides decisions within firms, ethics helps guide the law. Law and business ethics serve as an interactive system—informing and assessing each other. For example, our ethical inclination to encourage trust, dependability, and efficiency in market exchanges shapes many of our business laws. The principles of contract law, for instance, facilitate market exchanges and trade because the parties to an exchange can count on the enforceability of agreements. Legal rules that govern the exchange have been shaped in large part by our sense of commercial ethics.

At this point it might be helpful to get a stronger sense of the range of ethical and unethical business behavior by studying the chart in Exhibit 2-2.

Exhibit 2-2 Examples of Unethical and Ethical Business Executives and Businesses



The Complexity of Business Ethics: The Story of Two Biotech Ceos

Elizabeth Holmes is a 37-year-old billionaire whose company, Theranos, claimed to be developing a technique for doing medical diagnostic work with the draw of a single drop of blood. The objective is to create a low-priced, less painful alternative to the large blood draws that have been the traditional way to do medical diagnoses.

Holmes claimed to be designing and producing a product that is so cheap that a person can get a cholesterol test for the price of an egg McMuffin. She proudly says that she will not raise prices and will not deny access to this new technology to people in need.

Yet, in an investigative report in the fall of 2015, *The Wall Street Journal* revealed that Theranos was doing some medical diagnostic work using standard blood drawing technology rather than their own highly touted techniques. In addition, the FDA announced that the Theranos innovation had not been adequately peer reviewed and was not an approved blood collection device.

In January 2022, Holmes was convicted of four counts of fraud.

Martin Shkreli is the founder and CEO of Turning Pharmaceuticals. He is a year older than Ms. Holmes and has an estimated wealth of \$100 million. He acquired the drug Daraprim, which is used by HIV and cancer patients, and promptly raised the price from \$13.50 to \$750. In interviews, he explained that he probably should have raised the price even more because those who needed the drug would be willing to pay even more because it was so valuable for their health. Daraprim costs approximately \$1 to make.

Turning gives away 60% of Daraprim to those who do not have the money to pay for it. Shkreli points out that his primary responsibility is to make profits for those who own Turning. On December 17, 2015, Shkreli was arrested on charges of securities fraud for allegedly using assets from a biotech company he started to pay off unrelated business debts.

Of course, different ethical understandings prevail in different countries. Thus, ethical conceptions shape business law and business relationships uniquely in each country. Increasingly, business leaders require sensitivity to the differences in legal guidelines in the various countries in which they operate. These differences are based on somewhat different understandings of ethical behavior among business people in diverse countries.

As we mentioned earlier, business ethics does not yield one correct decision. So how are business managers to chart their way through the ethical decision-making process? Consider the careers of two young entrepreneurs in Silicon Valley as additional insights into the complexity and necessity of business ethics. Are they ethical models? What more would you have to know about each of them before deciding whether future business leaders should try to follow their examples?

Ethical Failures Can Be Bad for Business

As the box above suggests, business behavior that might look attractive for profits can be a nightmare for a firm and the business leaders involved in making the decisions that led to the questionable behavior. For example, in 2016 a report documented that Wells Fargo employees had opened more than 2 million accounts for customers without their permission, and often applied fees and other charges to these extra accounts without the customers knowing. An investigation revealed that Wells Fargo employees were under extreme pressure from the company to meet certain sales quotas, and often the only way to meet these quotas was to fraudulently open extra accounts.

Wells Fargo was required to return \$2.6 million to consumers and, due to the severity of Wells Fargo's wrongdoing, the Consumer Financial Protection Bureau (CFPB) ordered Wells Fargo to pay the largest fine the CFPB has ever imposed, \$185 million. In addition, Wells Fargo CEO John Stumpf stepped down from his position as a result of the scandal.

Perhaps what is most interesting about this case, however, is the scope of the reaction that it inspired. Not only did the CFPB order an enormous fine, but several U.S. cities, including Seattle, Chicago, and Sacramento, largely or entirely divested their funds from Wells Fargo accounts in protest over the scandal. This largely unprecedented move may represent a growing demand for business accountability and transparency, among public and private consumers alike.

Another well-known 2016 business ethics case involved the drug company Mylan and its EpiPen product. An EpiPen is a pocket-sized device used for the self-injection of epinephrine, an antidote

for anaphylactic shock brought on by allergy reactions. Having access to an EpiPen can truly be a matter of life or death for someone prone to extreme allergic reactions. Thus, when Mylan suddenly increased the price of an EpiPen by 500 percent, making the price of each EpiPen pack \$600, there was a strong outcry from consumers, especially considering that generic alternatives to the device were practically nonexistent. Several state attorneys general launched fraud and antitrust investigations, and the House Oversight Committee got involved as well, in the form of a hearing with Mylan's CEO. The bad publicity sank Mylan's stock, and Mylan eventually reduced the price of the EpiPen (although the price remains relatively high compared to the original price).

What is your reaction to Chevron's behavior in Ecuador? How do we begin to think about what is right and wrong in a situation like this one?

The starting point in wrestling with dilemmas about what is right and good is the idea of values.

What Are Values?

LO 2-3 Define values.

values

Positive abstractions that capture our sense of what is good and desirable.

When we think about the ultimate reason or purpose for which we make decisions in a business firm, we turn to the basic unit of business ethics—values. **Values** are positive abstractions that capture our sense of what is good or desirable. They are *ideas* that underlie conversations about business ethics. We derive our ethics from the interplay of values. Values represent our understanding of the purposes we will fulfill by making particular decisions.

For example, we value honesty. We want to live in communities where the trust we associate with honesty prevails in our negotiations with one another. Business depends on the maintenance of a high degree of trust. No contract can protect us completely against every possible contingency. So we need some element of trust in one another when we buy and sell.

Take a look at American Express's core values listed in Exhibit 2-3. Think about how each abstraction would play out through the business's behavior.

If we think about the definition of values for a moment, we realize two things. First, a huge number of values pull and push our decisions. Second, to state that a value is important in a particular situation is to start a conversation about what is meant by that particular value. To return to the Chevron case, when someone says we wanted to maximize efficiency, environmental sustainability, or justice, we are only slightly closer to any understanding of the complexity of the dilemma.

Sometimes a firm's core values seem less ambiguous, but they still leave a lot of ambiguity and flexibility for business decision making. See Adidas's core values in Exhibit 2-4 as an example.

Sometimes, staying true to a company's values can mean making decisions that do not necessarily seem good for business. For example, the pharmacy chain CVS considers itself in the business of health care and prides itself on "helping people on their path to better health." However, CVS also sold cigarettes—a product long known to cause serious health problems. So, in 2014, CVS's CEO Larry Merlo made the tough decision to stop selling cigarettes at every single CVS location across the nation. Merlo knew that this decision could have substantial costs for CVS as smokers took

Exhibit 2-3

American Express's
Core Values

AMERICAN EXPRESS'S CORE VALUES

- Customer Commitment
- Quality
- Integrity
- Teamwork
- Respect for People
- Good Citizenship
- A Will to Win
- Personal Accountability

ADIDAS'S CORE VALUES

- We are committed to continuously strengthening our brands and products to improve our competitive position.
- We are consumer-focused and therefore we continuously improve the quality, look, feel and image of our products and our organizational structures to match and exceed consumer expectations and to provide them with the highest value.
- We are innovation and design leaders who seek to help athletes of all skill levels achieve peak performance with every product we bring to market.
- We are dedicated to consistently delivering outstanding financial results.
- We are a global organization that is socially and environmentally responsible, that embraces creativity and diversity and is financially rewarding for our employees and shareholders.

Exhibit 2-4

Adidas's Core Values

their business elsewhere, but he stated that “[e]nding the sale of cigarettes and tobacco products at CVS Pharmacy is simply the right thing to do for the good of our customers and our company.” By making this move, CVS also firmly established its dedication to health in the minds of its customers. Balancing values and profits is never easy, but it can be integral to running a successful business.

How Do Values Provide a Starting Point for Thinking about Business Ethics?

LO 2-4 Explain how values provide a starting point for thinking about business ethics.

To help make WH useful to you as a manager, Exhibit 2-5 makes clear the central role of clarifying what version of a value one feels loyalty toward. Without that clarification, we lose sight of why something is said to be good or right. The exhibit identifies four of the most important values influencing business ethics and presents alternative meanings for each. This table should not only help clarify the importance of values in your own mind but also enable you to question others who claim to be acting ethically. For instance, a manager might be deciding whether to fire an employee

VALUE	ALTERNATIVE MEANINGS
Freedom	1. To act without restriction from rules imposed by others 2. To possess the capacity or resources to act as one wishes 3. To escape the cares and demands of this world entirely
Security	1. To possess a large-enough supply of goods and services to meet basic needs 2. To be safe from those wishing to interfere with your property rights 3. To achieve the psychological condition of self-confidence to such an extent that risks are welcome
Justice	1. To receive the products of your labor 2. To treat all humans identically, regardless of race, class, gender, age, and sexual preference 3. To provide resources in proportion to need 4. To possess anything that someone else is willing to grant you
Efficiency	1. To maximize the amount of wealth in society 2. To get the most from a particular output 3. To minimize costs

Exhibit 2-5

Primary Values and Business Ethics

BUSINESS Ethics Flashpoint 2.2

Dole Food Company and Its Workers

Dole Food Company (Dole) dominates the market for bananas, holding a 25 percent share in the world market. The majority of bananas from Dole come from Latin America. Specifically, Dole operates banana plantations in several Latin American countries, including Ecuador, Nicaragua, Costa Rica, Guatemala, Honduras, and Panama.

An important step in the process of growing bananas is the application of pesticides to prevent disease and pathogens. Fumazone was among the most toxic pesticides used in banana cultivation during the 1960s through the 1980s.

The main ingredient in Fumazone is dibromochloropropane (DBCP). DBCP is known to have harmful effects on male reproductive organs and sperm counts. However, despite knowledge of this danger, the U.S. government approved its use on farms in 1964.

During a brief period after 1964, about 60 workers in California that manufactured Fumazone were found to be sterile. As a consequence, in 1979, the U.S. Environmental Protection Agency banned the use of DBCP in the United States. However, Dole continued using DBCP in its Latin American plantations well into the mid-1980s.

Dole admitted to knowing that DBCP could harm the workers but chose not to inform its workers in Latin America. As a consequence of Dole's use of DBCP on its plantations, the health of Latin American plantation workers was threatened.

DBCP posed a health hazard to plantation workers in that it was known to cause male sterility as well as genetic disorders in the children of men and women exposed to DBCP. In fact, the National Institutes of Health claims that DBCP is toxic, carcinogenic, and mutagenic. Further, the State of California's Safe Drinking Water and Toxic Enforcement Act of 1986 concluded that DBCP caused reproductive and developmental harm.

Although the toxicity of DBCP was well-known, banana plantation workers were reportedly not given equipment or training to minimize exposure to the harmful chemical. Unfortunately, the task of applying DBCP on banana plants

fell to the most marginalized of workers because few workers desired to risk exposure to DBCP.

Another problem with DBCP is that it negatively affected the environment. For example, the application of Fumazone to banana roots caused DBCP to seep into the groundwater. This contamination of the environment killed organisms living in the surrounding habitat, including fish, mammals, and plants.

In 2004, a small breakthrough was made. Twelve banana plantation workers filed a suit against Dole in a California court. Six of these workers were found to have been made sterile due to the poor working conditions of Dole's banana plantations. During these proceedings, evidence was presented showing that Dole knew that DBCP could harm the workers and nevertheless insisted on using DBCP. In addition, Dole had ignored safety recommendations by the manufacturer of the pesticide Fumazone.

On November 5, 2007, the suit filed by the 12 workers resulted in Dole being ordered to pay damages to 6 of the 12 workers. Specifically, the Los Angeles Superior Court awarded the plantation workers \$3.3 million in damages.

On November 15, 2007, a jury ordered Dole also to pay \$2.5 million in punitive damages to five of the workers—that is, damages paid in excess of the plaintiffs' proved injuries. Later, however, a judge vacated the punitive damages and lowered the actual damages of \$3.3 million to \$1.58 million.

As a result of the use of DBCP on banana plantations, thousands of banana pickers have filed suits against produce companies, such as Dole Food Co., Chiquita Brands International Inc., and Fresh Del Monte Produce Inc., and chemical companies, such as Dow Chemical Company and Shell Chemical Company.

However, thousands of workers continue to suffer from their work in the banana industry in Latin America. In addition, many of the banana workers are children; roughly 70 percent of these children work on Dole plantations, according to a Human Rights Watch report.

Sources: Armin Rosencranz, Stephen Roblin, and Nicole Balloffet, "Doling Out Environmental Justice to Nicaraguan Banana Workers: The Jose Adolfo Tellez v. Dole Food Company Litigation in the U.S. Courts," 3 Golden Gate U. Envtl. L.J.161 (2009); Human Rights Watch, "Ecuador: Widespread Labor Abuse on Banana Plantations," April 25, 2002, HRW.org.

whose performance is less than impressive. In making the decision, the manager explores alternative visions of key values such as justice and efficiency and then makes choices about which action to take. Values and their alternative meanings are the foundation for different ethical decisions.

Where do our value priorities come from? That question is another way of asking: At the foundational level, what causes us to place a higher weight on decisions that reflect some values rather than others?

Value priorities can stem from many sources. Tradition, family, culture, reasoning about the consequences of alternative choices, and a sense of duty or obligation can all fuel the value priorities we bring to an ethical dilemma.

For many people, their preeminent values derive from religious teachings. For example, Catholic social doctrine teaches that the moral quality of a society depends on how it treats



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Alamy Stock Photo

GLOBAL Context

Business Ethics and Swedish Advertising Law

Recall from the WH approach to ethical decision making that when businesses make decisions, they should consider *all* the relevant stakeholders. One relevant stakeholder is the customer, or consumer. In Sweden, consumers are assumed to be vulnerable in the marketplace; therefore, protecting the consumer is considered the job of the government. Unlike in the United States, in Sweden public policy acknowledges that “there exist large groups of consumers who, owing to low incomes, deficient education and knowledge of the market, etc., are less well equipped than the average citizen for their role as consumers.” One group of consumers less equipped than the average citizen in Sweden is children.

The government considers children extra vulnerable and impressionable and thus in need of even more protection than the average consumer. Swedish laws ban all television advertising targeting children below the age of 12. The ban includes not only toy advertisements but also commercials for foods high in fat and sugar, such as sweets and fast food. Advertisements for such products can be aired if the targets of the advertisements are not children. For example, commercials for toys, sweets, and foods high in fat may be aired if they are designed to attract and inform adults as opposed to children. What may surprise many Americans is that almost 90 percent of Swedish advertising professionals are in favor of the ban on advertising to children because they recognize that such advertising is misleading since children do not understand the commercial nature and purpose of advertising.

its most vulnerable members. Similarly, the United Methodist Church in its 2009–2012 Social Principles document pledges Methodists “to support the poor and challenge the rich.”

Try to express the struggle between Dole and its workers as a struggle between two sets of values rather than simply a contest between people in white hats and villains in black hats. If you can, you will be more fair in your assessment of Dole’s behavior. To be fair is not to condone but, rather, to be open to understanding the logic and purposes of all the relevant players in the ethical flashpoint.

The WH Framework for Business Ethics

LO 2-5 Analyze business decisions using the WH framework.

A useful set of ethical guidelines requires the recognition that managerial decisions must meet the following primary criteria (Exhibit 2-6):

- The decisions affect particular groups of stakeholders in the operations of the firm. The pertinent question is, thus, *whom* would this decision affect?
- The decisions must meet the standards of action-oriented business behavior. Managers need a doable set of guidelines for *how* to make ethical decisions.

stakeholders

The groups of people affected by a firm’s decisions.

Exhibit 2-6

The WH Process of Ethical
Decision Making

Who Are the Relevant Stakeholders?

The **stakeholders** of a firm are the many groups of people affected by the firm’s decisions. Any given managerial decision affects, in varying degrees, the following stakeholders:

1. Customers.
2. Owners or shareholders.
3. Management.
4. Employees.
5. The general community where the firm operates.
6. Future generations.

Managers should make sure they consider all relevant stakeholders when they engage in ethical reasoning.

1. W—WHO (Stakeholders)

Customers
Owners or shareholders
Management
Employees
Community
Future generations

2. H—HOW (Guidelines)

Public disclosure
Universalization
Golden rule

BUSINESS Ethics Flashpoint 2.3

The WorldCom Accounting Scandal

WorldCom Inc. was a telecommunications company that began operating in the state of Mississippi in the 1980s. In 1989, WorldCom became a publicly traded corporation; that is, it began selling shares of its company to investors.

In the 1990s, WorldCom became the second largest U.S. long-distance telephone service carrier. In addition, it was a leading operator of Internet services and placed forty-second among the *Fortune* 500 companies in 2001.

As the 1990s came to an end, telecommunications was expanding and becoming more competitive. Numerous telecommunications companies entered the long-distance communications market, including the local telephone companies and the Regional Bell Operating Companies, and many companies entered the market for Internet services.

Eventually, the supply of telecommunications services outgrew the demand for those services, and the industry experienced a recession—that is, a drop in economic activity. WorldCom's revenue began to fall.

During this time, WorldCom used fraudulent accounting methods that allowed it to overstate its financial status to its shareholders. Specifically, CEO Bernard Ebbers presented a false picture of WorldCom's net worth, informing the Board of Directors of WorldCom that the company would continue growing vigorously. However, Ebbers knew that his projections were inconsistent with WorldCom's declining position.

One reason for boosting the reported revenues of WorldCom was to increase shareholder confidence. In other words, the logic behind Ebbers' fraudulent accounting methods was that if he could deceive shareholders into

believing that WorldCom was growing, shareholders would continue to inject money into the company.

The fraud at WorldCom was propagated not just by Ebbers but also by several other officials, including CFO Scott Sullivan and WorldCom's comptroller, David Myers. Both of these individuals aided in secretly making entries of hundreds of millions of dollars into WorldCom's accounting report without any basis for such entries.

The fraud committed by the executive officials at WorldCom resulted in overstating the company's income by \$11 billion.

In 2005, Ebbers was found guilty in federal court of fraud and received a sentence of 25 years in prison. Scott Sullivan received five years in prison, pleading guilty to fraud, conspiracy, and making false financial statements. David Myers received a sentence of one year and one day in prison.

As a result of the accounting fraud that occurred in the early 2000s, WorldCom was forced to declare bankruptcy. When this occurred, thousands of workers at WorldCom lost their jobs, and shareholders lost billions of dollars as the worth of WorldCom plummeted.

WorldCom not only affected its workers and shareholders but the entire telecommunications industry. Specifically, competing telecommunications companies that had once trusted WorldCom's false accounting reports now realized that they had been duped into relying on false data when making business decisions.

Sources: Dennis R. Beresford, Nicholas deB. Katzenbach, and C. B. Rogers, "Report of Investigation by the Special Investigative Committee of the Board of Directors of Worldcom, Inc." (March 31, 2003), FindLaw.com; Jennifer Bayot and Roben Farzad, "Ex-WorldCom Officer Sentenced to 5 Years in Accounting," August 12, 2005, NYTimes.com.

Study Business Ethics Flashpoint 2.3. First, identify the stakeholders directly affected by the behavior of WorldCom and then tackle the harder task of identifying the many stakeholders who are in the background, perhaps, but were nevertheless affected immensely by WorldCom's actions.

Some of the more perplexing ethical dilemmas have emerged as a result of our increasing dependence on e-commerce.

How Do We Make Ethical Decisions?

Making ethical decisions has always been one of our most confusing *and* important human challenges. In the process of meeting this challenge, we have discovered a few general ethical guidelines to assist us. An *ethical guideline* provides one path to ethical conduct. Notice that all three of the ethical guidelines (the golden rule, public disclosure test, and the universalization test) reflect a central principle of business ethics: consideration of stakeholders.

E-COMMERCE and the Law

Technological Records and Ethics

Journalists use different technological media to contact and store information about confidential sources, including government whistleblowers. One of the most important parts of journalism is to protect confidential informants so that news sources can still enlighten the public with important and sensitive information. Ethical issues arise from this challenge. Documents containing information about informants' identities may not be collected by the government without permission from the Deputy Attorney General. In other words, the First Amendment protects the privacy and individual ownership of these email and phone records.

For example, in 2004, the Federal Bureau of Investigation (FBI) illegally obtained phone records related to the confidential informants of *The New York Times*' and *Washington Post*'s bureaus in Indonesia. The executive editors of both newspapers were called by the FBI, and both received

apologies. The Justice Department looked into the illegal investigation by the FBI after the FBI went ahead with what it called "emergency" gathering of private information related to an alleged terrorist investigation. The editors were never told why their records were needed.

Now, news corporations are putting numerous security barriers and encryptions around their records so that nobody could have access to them even if they tried. In fact, Wikileaks, the website that publicizes secret government documents, has probably the strongest security procedures protecting its sources. Instant messages are expertly encrypted, as are all files passed between people. A tool that enables users to communicate completely anonymously, the Tor Project, completely hides all servers. Other news companies are attempting to mimic such standards and adjust privacy policies to reserve the right not to release any information about a source "to law enforcement authorities or to a requesting third party without notice."



CASE Nugget

Tyson Foods' Bribery Charges

In 2004, memos containing information regarding illegal bribes were sent from a Tyson Foods plant manager in Mexico to corporate officials in the United States. Basically, company officials in Mexico were sending roughly \$2,700 a month to the wives of two veterinarians involved in safety and quality of the food produced at the plant. At the time, Tyson Foods was attempting to increase its national export. However, countries involved in the importation of these products require experts to certify that these food products meet certain safety and sanitary standards. Essentially, the two veterinarians were being sent extra payments so that they would sign off on the quality of the products produced at the plant regardless of whether the products were actually up to par with the standards imposed. This act is especially dangerous considering the reputation poultry products have of passing on disease, including salmonella, to consumers.

The company officials in Arkansas, including the president of Tyson International and vice president of operations, realized that bribing foreign officials, the biggest issue at hand, was a felony according to the Foreign Corrupt Practices Act. Faced with the option of investigating the allegations and bringing the illegal activities to light, the company officials instead found a way to keep sending the bribes but make the payments look legal. Two years later, Tyson officials finally hired a law firm to do an internal investigation of the bribery. In 2011, Tyson was charged with conspiracy and violating the Foreign Corrupt Practices Act. To avoid trial, Tyson was forced to pay \$4 million as a criminal penalty and \$1.2 million to the Securities Exchange Commission for the charge of maintaining illegal records.

BUSINESS Ethics Flashpoint 2.4

The Health Focus of Revolution Foods

Revolution Foods started as a small business venture in Oakland, California. The start-up's objective is to provide healthy prepackaged lunch meals for children.

Currently, the market for prepackaged lunch meals is dominated by Kraft Foods. Kraft Foods sales of Lunchables account for approximately 76 percent of sales in the prepackaged lunch market niche.

Kids love Lunchables because these meals allow them to create their own food. Simply, these meals are fun. Parents also benefit from Lunchables in the sense that these meals require no preparation.

However, Lunchables are not necessarily healthy. According to food critics, including the founders of Revolution Foods, Lunchables contain an excess of fat, sugar, salt, and preservatives that are unhealthy.

For example, Kraft previously had a Maxed Out line of Lunchables that was considered one of the Five Worst Packaged Lunchbox Meals by the Cancer Project. Kraft eventually stopped producing this line of Lunchables—with a whopping 660 calories and 22 grams of fat—and endeavored to create more healthy meals.

In response to the apparent need for more nutritious lunch kits, Revolution Foods claims to offer a healthy alternative.

Kristin Richmond, one of the founders of Revolution Foods, believes that the objective of Revolution Foods is to

provide higher-quality ingredients to cultivate healthier lifestyles. Making foods with real meat, real cheese, and other recognizable ingredients appears to be the driving force behind the company.

In other words, rather than focusing solely on profits, Revolution Foods attempts to focus on what will also help the consumer lead a healthier lifestyle.

One example of the types of prepackaged lunch kits that Revolution Foods offer is the Ham and Cheddar Meal Kit, consisting of ham from animals raised with no antibiotics. This lunch kit also has no preservatives, no high-fructose corn syrup (a commonly used artificial sweetener), and no artificial coloring.

On average, Revolution Foods' Meal Kits are lower in fat, salt, and sugar than Kraft's Lunchables.

The director of nutrition policy at the Center for Science in the Public Interest has claimed that Revolution Foods, although not necessarily healthy, is nutritionally improved. The fact that Revolution Foods provides foods that are locally grown, natural, and organic without preservatives appeals to those consumers who desire to cultivate healthy dietary habits.

Revolution Foods' Meal Kits can now be found in more than 1,000 stores, including Kroger's, Target, and Whole Foods.

Sources: Stephanie Strom, "Lunchables, The Lunchbox King, Faces a Rival Vowing Higher-Quality Fare," *N.Y. Times*, August 21, 2013; Marc Gunther, "Revolution Foods: a healthier competitor to Lunchables," March 11, 2014, *The Guardian.com*.

The Golden Rule The idea that we should interact with other people in a manner consistent with the way we would like them to interact with us has deep historical roots. Both Confucius and Aristotle suggested versions of that guideline. One scholar has identified six ways the Golden Rule can be interpreted:

1. Do to others as you want them to gratify you.
2. Be considerate of others' feelings as you want them to be considerate of yours.
3. Treat others as persons of rational dignity like you.
4. Extend brotherly or sisterly love to others, as you would want them to do to you.
5. Treat others according to moral insight, as you would have others treat you.
6. Do to others as God wants you to do to them.

Regardless of the version of the Golden Rule we use, this guideline urges us to be aware that other people—their rights and needs—matter. The focus on others that is the foundation of the Golden Rule is also clearly reflected in a second ethical guideline: the public disclosure test.

Public Disclosure Test One way to think of the public disclosure test is to view it as a ray of sunlight that makes our actions visible rather than obscured. The public disclosure test is sometimes called the television test, for it requires us to imagine that our actions are being broadcast on national television. The premise behind this general guideline is that ethics is hard work, labor

BUSINESS Ethics Flashpoint 2.5

The Dofasco Steel Company's Approach to Workers

Dofasco is the second-largest steel producer in Canada and sells a wide range of steel products. In the 1980s, Dofasco experienced shrinking profits and decided to change its approach to business.

One of the ways that Dofasco changed was in its approach to its workers. Specifically, Dofasco attempted to implement a philosophy taking into account the whole person at work. In other words, this approach sought to include wellness as an important characteristic of the employee experience.

In line with this new philosophy, the Dofasco management claimed it would abide by the following policy statement issued in its 1996 guides of the company's health, safety, and lifestyle activities: "At Dofasco, there is nothing more important than the health and safety of our people."

Consistent with this policy statement, Dofasco provided training for employees in problem solving, manufacturing processes, and customer service. Dofasco also built on its tradition of providing its workers with ergonomic and fitness resources as well as preventive medical services.

Yet another way that Dofasco sought to focus its energies on employee needs was by encouraging healthy lifestyle practices at work. A healthy lifestyle at work would be achieved by preventing workplace accidents and maintaining a safe environment. In addition, Dofasco assessed employee needs in response to worker suggestions.

Dofasco believes that its focus on a safe and healthy workplace has improved its business. Specifically, the company claims that its policies have reduced lost time associated with work injuries and minimized Workers Safety Insurance Board payments.

In addition to focusing on worker safety and well-being, Dofasco also has a history of being environmentally responsible. For example, Dofasco was the first corporation in Canada voluntarily to sign an Environmental Management Agreement with Environment Canada and Ontario's Ministry of the Environment. In this agreement, Dofasco made commitments to abide by specific air and water quality standards and sustainable energy use and waste management. Through this agreement, Dofasco expressed its commitment to the community.

In addition, Dofasco created a Sustainable Development Strategy Team and is a founding sponsor of the Sustainable Enterprise Academy at York University's Schulich School of Business. The mission of this academy is to provide executives with training in how to manage businesses with an eye for sustainability.

Dofasco's organizational practices resulted in being named one of the world's most sustainable companies in the Dow Jones Sustainability Group Index.

Sources: Dan Corbett, "Excellence in Canada: Healthy Organizations—Achieve Results by Acting Responsibly," *Journal of Business Ethics* 55, no. 2 (December 2004), pp. 124, 130; Joan Enric Ricart, et. al. "The Sustainable Enterprise: Learning from DJSI Leaders," *Fundacion BBVA* (2005).

that we might resist if we did not have frequent reminders that we live in a community. Given our role as a member of a community, our self-concept is tied, at least in part, to how that community perceives us.

Universalization Test A third general guideline shares with the other two a focus on the "other"—the stakeholders whom our actions affect. Before we act, the **universalization test** asks us to consider what the world would be like if our decision was copied by everyone else. Applying the universalization test causes us to wonder aloud: "Is what I am about to do the kind of action that, if others followed my example, makes the world a better place for me and those I love?"

This chapter concludes with two Business Ethics Flashpoint examples: Flashpoints 2.4 and 2.5. For the first one, try to word what the firm did in terms of the ethical guidelines. Did its behavior show potential consistency with all three of the guidelines?

As you study this next Business Ethics Flashpoint, start by asking yourself what values are in conflict in this business scenario. After you have established which values are in tension, work through both steps in the WH process for making ethical business decisions.

In summary, business managers can apply the WH approach to most ethical dilemmas. The WH framework provides a practical process suited to the frequently complex ethical dilemmas that business managers must address *quickly* in today's society.

universalization test

The ethical guideline that urges us to consider, before we act, what the world would be like if everyone acted in this way.

Point/Counterpoint

The Social Responsibility of Corporations

Do a Firm's Ethical Responsibilities Extend Beyond Maximization of Profits?	
YES	NO
Communities have dozens of needs that, when met, assist citizens in flourishing. What sense does it make to take an important sector like corporate America and deny them the opportunity to assist in meeting these needs? When a computer firm decides to enhance the educational mission of the town where they produce their product by giving computers to the school, they do so in an environment where schools are often pinched for funds. Those students need computers, and they would take them from anyone who is kind enough to provide them. Business firms are major citizens. They require utilities, roads, airports, police, sewage systems, power plants, and fire protection. These services impose heavy costs on the community. Firms, like other citizens, have a responsibility to assist in paying for these public services. Their tax payments certainly serve this purpose. But from the community's perspective, should we not encourage citizens of all kinds to give back to their communities as often and as generously as they are willing to provide? Applauding the social responsibility of firms when they give back to their communities strengthens the ties of the firm to that community. A sense of mutual respect blooms between the corporation and the community where so many of its managers and workers have agreed to live.	The basic purpose of a business firm is to provide a service or product to consumers that makes profits for its owners. Capitalist theory depends on the incentive of the profit motive as a guarantee that firms will meet the desires of consumers. Please those consumers, and the market is an outstanding institution. Displease them, and you go out of business. This sanitizing process relies on the assumption that firms will seek to maximize profits. When firms decide for themselves that they will have goals that conflict with profit maximization, they undercut the meaning and the benefits of capitalism. Democracies have a process for deciding which of the countless potential good deeds a community will pledge to do. Tax money is never bountiful enough to satisfy our human desire to assist one another. We must pick and choose which needs to meet and which to postpone for another day. But the point is that we make these decisions AS A COMMUNITY. When a corporation takes it upon itself to use money it earned by charging consumers a price for a good or service, that firm is seizing the role of government BECAUSE IT CAN. No community has ceded the right to make social decisions to the corporation. Instead, the firm uses its powers to spend the community's money AS THE CORPORATION SEES FIT. This behavior is an affront to democracy and basically says to the community, "We know best what the community's priorities should be." If firms have so many excess profits that they can become a "good deeds" agency as well as a business firm, they should honor their true role and lower prices so more consumers can buy their products. By being what they claim is socially responsible, they are implicitly taxing their consumers who pay for a good or service AND then an extra fee for the firm to do what it designates as our top social priorities.

Questions & Problems

1. What ethical guidelines could help an American business manager working in another country decide whether she should engage in behavior that is ethical where she works but unethical in the United States?
2. What is the relationship between business behavior that is legal and business decisions that are ethical?
3. How do business ethics and business law interact with each other?
4. How does the WH approach to ethics respond to an ethical problem?
5. In 2000, Donald Stern incorporated a startup company named Grail in order to market a new and revolutionary chip design that Stern had invented. While witnesses expressed the view that Stern's innovation would be the "Holy Grail of memory technology," the company was unable to find investors, and by March,

2001, Grail had run out of money. On April 19, 2001, the following month, Stern met with Ryuichi Matsuo and Kazutoshi Hirayama, two representatives from Mitsubishi. Matsuo signed a nondisclosure agreement which required Mitsubishi “to keep in strict confidence and trust and not use, disclose or make available to others, including any of its affiliates or third parties any ‘Proprietary Information’ and ‘Company Documents and Materials’ (together ‘INFORMATION’) without the prior written consent of [Grail].” In the meeting, Stern showed Hirayama 16 items of proprietary information, including the core concept behind his miracle memory chip, of which Hirayama took extensive notes. Nothing came from the meeting between Grail and Mitsubishi.

In 2003, Mitsubishi and Hitachi formed Renesas Technology in a joint venture. Hirayama was one of the employees transferred from Mitsubishi. Stern suspected that Renesas was using his innovations and that Mitsubishi had broken the NDA because of an article he read promoting Renesas’ new technology. In the ensuing 2012 trial, expert witnesses found that “of the 16 items of confidential information disclosed to Mitsubishi, 11 had been implemented” in Renesas’ new technology. On May 16, 2012, the jury found that Mitsubishi had violated the NDA and determined damages to be \$123,898,889. Mitsubishi has filed an appeal for a new trial to address the damages, which is ongoing now.

How would Mitsubishi’s violation of the NDA affect the decisions of other innovative tech companies to approach potential investors?

Which aspects of the WH process did Mitsubishi neglect in their decision to break the NDA?

Source: *Grail Semiconductor, Inc. v. Mitsubishi Electric & Electronics USA, Inc.*, 225 Cal. App. 4th 786 (2014).

6. Tyco International, a manufacturing company, sued its former CEO, Dennis Kozlowski, in regard to his receipt of unauthorized bonuses from the company profits. Among his other wrongdoings, Kozlowski awarded unauthorized special bonuses to himself and more than 40 other Tyco employees. In sum, he misappropriated from company funds over \$100 million that he was not authorized to receive. Included in this misappropriation was the use of company funds for personal expenditures, such as \$18 million to buy and redecorate his New York City apartment and \$1 million for his wife’s 40th birthday party, held on the Italian island of Sardinia. The extravagant party featured an ice sculpture of the statue of David urinating Stolichnaya vodka. Based on these and other corporate misdeeds in related criminal proceedings, Kozlowski is currently serving 8.33 to 25 years at the Mid-State Correctional Facility in New York. How do

you think Kozlowski would have acted had he considered the public disclosure test before engaging in these corporate misdeeds? What if he applied the universalization test?

Source: *Tyco Intl, Ltd. v. Kozlowski*, 2005 DNH 68; 2005 U.S. Dist. LEXIS 6867 (April 21, 2005).

7. In Arkansas, methamphetamine (meth) was manufactured primarily in small toxic labs (STLs) located in homes, tents, barns, or hotel rooms. According to the plaintiffs (a number of counties in Arkansas), Arkansas had one of the highest numbers of STLs in the nation. The counties alleged that they had spent significant amounts of taxpayer dollars combating the manufacture of methamphetamine, including law enforcement costs for locating, eliminating, and cleaning up STLs; prison and jail costs for housing illegal users, dealers, and manufacturers; addiction treatment costs for users and addicts; payments to family service agencies for housing and treating children whose parents were arrested on meth-related charges; and costs for treating the physical side effects of meth use and exposure to its production. To recoup these costs, the plaintiffs sought compensation from Pfizer, Inc., and other manufacturers of cold and allergy medicines. They brought the suit against these manufacturers because meth cannot be produced without ingredients from their cold and allergy medicines. What ethical duties, if any, do you think the drug manufacturers owe to the state or people in this case? Apply the WH framework to help reach your conclusions.

Source: *Ashley County et al. v. Pfizer, Inc.*, 552 F.3d 659; 2009 U.S. App. LEXIS 19.

8. Todd Russell Dolezal is a bail bondsman who was slapped with a misdemeanor, a \$1000 fine, and a probationary period of one year for soliciting bail in violation of California Code of Regulations, title 10, 170*170 section 2079.1. Section 2079.1 bans bail bondsmen from directly soliciting bail in jail facilities or court facilities. Furthermore, “any solicitation [regarding bail] of an arrestee himself. . . shall be only after a bona fide request for bail services has been received from the arrestee. . .” In 2013, Dolezal tried to appeal on grounds that the regulation violated his First Amendment right, but the appeals court affirmed the previous result.

What purpose does section 2079.1 serve within the context of the WH process? Who does this law protect? Why would a law like this be necessary?

Source: *People v. Dolezal*, 221 Cal. App. 4th 167 (2013).

9. Dragon, a speech recognition technology company considered to be “a leader in speech technology products” and valued at \$600 million, was in perilous straits. Despite being valued so highly, the

company lost money in every year of its existence except for one year. Dragon was sorely in need of capital. Dragon considered merging with another company to sustain itself until it could develop its technologies further and make them profitable. To go about this business, Dragon entered into a contract with Goldman Sachs on December 8, 1999, to “provide [Dragon] with financial advice and assistance in connection with this potential transaction, which may include performing valuation analysis, searching for a purchaser acceptable to [Dragon], coordinating visits of potential purchasers and assisting [Dragon] in negotiating the financial aspects of the transaction.”

Goldman formed a four-member team to conduct financial due diligence on Lernout & Hauspie Speech Products N.V. (“L & H”), a company that had offered to buy Dragon for \$580 million paid in stock. Goldman’s assessment of L & H was “positive in the overall” but “did not give an opinion pro or con on the transaction.” In June 2000, the Dragon board approved the merger with L & H and ceased to become an independent entity.

Unfortunately for the ex-board members of Dragon, *The Wall Street Journal* reported that L & H had vastly overstated its revenues in an August 2000 article. The SEC promptly began investigating L & H’s financial statements. L & H had improperly recorded \$373 million in revenue and was forced to restate its financials for the past two and a half years. In November 2000, L & H filed for bankruptcy and the share of L & H stock used to pay for the merger became worthless.

Naturally, the ex-board members of Dragon took Goldman Sachs to trial for negligent performance of services, gross negligence, and intentional and negligent misrepresentation, among other claims. However, the court ruled in favor of Goldman on January 23, 2013, and an appeal for a new trial by the plaintiffs on the grounds of evidentiary errors and erroneous jury

instructions was rejected by the First Circuit Appeals Court on November 12, 2014.

L & H’s fraudulent actions obviously caused harm to the shareholders of Dragon. Who are some less obvious stakeholders, as defined by the WH Process, that were negatively affected by L & H?

During the trial, it was noted that Goldman’s team had not disclosed their concern about the status of due diligence of L & H to Dragon because “the client did not ask.” How ethical was this course of action?

Source: *James and Janet Baker; Paul G. Bamberg and Robert Roth v. Goldman, Sachs & Co.*, 771 F.3d 37 (1st Cir. 2014).

10. Titan Distribution Inc. had subcontracted with a company that provided employees, but Titan later decided to hire its own employees and end the subcontracting contract. Robert Chalfant worked for the subcontracted company, and when Titan made this change, Chalfant sought the same position with Titan that he had held while employed by the subcontractor. Although Titan initially indicated that Chalfant passed his physical examination and would be hired, the company subsequently decided that he failed the physical and did not hire him. The evidence indicated that Titan mistakenly believed that Chalfant’s physical ailments substantially limited his ability to work, that he previously performed and remained able to perform the functions of the job, and that the refusal to hire him on the basis of the allegedly failed physical was linked to his disability. Further, Titan’s inconsistent and unexplained decision-making process, with knowledge of the federal discrimination laws, was sufficient to support an award of punitive damages. Later you will learn about discrimination, but right now, consider the ethical issues of this case. What values are at odds in the dilemma outlined in this case?

Source: *Chalfant v. Titan Distribution, Inc.*, 475 F.3d 982 (2007).

Steer the Ship

Have you ever stopped to think about how your favorite shoes got to market? Research and development, manufacturing, supply chain, marketing, and finance all had a role in the process. Do you know who had a role in every one of those functions? The legal team.

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