

Leadership Ethics and Social Responsibility

LEARNING OBJECTIVES

After studying this chapter and doing the exercises, you should be able to

- Specify key principles of ethical and moral leadership.
- Apply a guide to ethical decision making.
- Present representative examples of unethical behavior by business leaders.
- Describe what leaders can do to foster an ethical and socially responsible organization.
- Explain the link between business ethics and organizational performance.

CHAPTER OUTLINE

Principles and Practices of Ethical and Moral Leadership

Four Ethical Leadership Behaviors
Factors Contributing to Ethical Differences
The Ethical Mind for Leaders

Guidelines for Evaluating the Ethics of a Decision

A Sampling of Unethical Leadership Behaviors

Leadership, Social Responsibility, and Creating an Ethical Organizational Culture

Providing Strategic Leadership of Ethics and Social Responsibility
Creating a Pleasant Workplace
Helping Build a Sustainable Environment
Engaging in Social Entrepreneurship
Engaging in Philanthropy
Working with Suppliers to Improve Working Conditions

Establishing Written Codes of Ethical Conduct
Developing Formal Mechanisms for Dealing with Ethical Problems

Accepting Whistleblowers
Providing Training in Ethics and Social Responsibility
Placing Company Interests over Personal Interests

Ethical and Socially Responsible Behavior and Organizational Performance

Summary

Key Terms

Guidelines for Action and Skill Development

Leadership Case Problem A

Leadership Case Problem B

Notes

Judy Chen, head of garment production at a clothing retailer for infants and children, was facing a dilemma caused by profit-margin squeezing pres-

ures. Major increases in cotton and labor costs were making it much more expensive to produce garments without raising prices. Many other apparel company executives

were upset by the increases in the cost of production because for a twenty-year period, production costs were stable or declining. The problem Chen and her counterparts in other companies faced was that budget-conscious consumers resisted higher prices.

Chen was familiar with the “deconstruction” approach several other apparel makers were taking to lower the price of producing a garment. The deconstruction approach involves some nipping and tucking to reduce the amount of fabric or buttons in a garment. In the manufacture of a pair of khaki pants that sold for about \$34, the company could save about 50 cents per garment through such measures as eliminating cuffs, pleats, and coin pockets and replacing a metal hook and bar clasp with a button.

One day Chen was contemplating which cost-cutting steps to implement in order to save about \$1 in the

manufacture of two of the best-selling pants for children—“Khaki Prince” and “Khaki Princess.” A deconstruction consultant suggested eliminating the coin pocket in the pants, reasoning that “What child or parent is going to notice the difference?” Chen thought about this particular cost savings of approximately 40 cents per garment, and she decided no. In her words, “First of all my own children, my nephews and nieces, and my neighbors’ children love the small coin pockets. Just the other day, I found two little stones in the pocket, along with a small twig and a nickel. Then I did the public knowledge test, and I asked myself how I would feel if there were a Twitter post that said, ‘Judy Chen saves company 40 cents per children’s garment by eliminating coin pocket’ We’ll find some other way to reduce manufacturing costs.”¹

In this chapter, we examine leadership ethics and social responsibility from several major perspectives: principles of ethical and moral leadership, an ethical decision-making guide, examples of ethical violations, examples of how leaders develop an ethical and socially responsible culture, and the link between business ethics and organizational performance.

Principles and Practices of Ethical and Moral Leadership

Enough attention has been paid to what leaders at all levels *should* do that some principles of ethical and moral leadership have emerged. Because terms dealing with the ideal behavior of leaders are used so loosely, it is helpful to define what these terms have generally come to mean in the business community. **Ethics** is the study of moral obligations, or of separating right from wrong. *Ethics* can also be a plural noun meaning the accepted guidelines of behavior for groups or institutions.² In this sense, it means much the same as **morals**, which are an individual’s determination of what is right or wrong; morals are influenced by a person’s values. Values are tied closely to ethics because ethics become the vehicle for converting values into action. A leader who values fairness will evaluate group members on the basis of their performance, not personal friendships. And a moral leader will practice good ethics.

Edwin A. Locke, the goal theorist, argues that ethics is at the center of leadership because the goal of a rational leader is to merge the interests of all parties so that everyone benefits and the organization prospers.³ The ethics link is that if everyone benefits, all people are being treated ethically.

In this section, we present a sampling of ethical and moral behaviors, all centering on the idea that a leader should do the *right* thing, as perceived by a consensus of reasonable people. None of these terms can be pinned down

with great precision. We also present a brief explanation of why the ethical and moral behavior of leaders differs so widely, and pay separate attention to the importance of an ethical mind. Before studying these principles, do Leadership Self-Assessment Quiz 6-1 to think through your work-related ethics and morality.



LEADERSHIP SELF-ASSESSMENT QUIZ 6-1

The Leadership Ethics Quiz

Directions: Circle the numbers to indicate how well each statement describes your current attitudes and behavior, or how you would behave if placed in the situation suggested by the statement. Response choices: 1 = disagree strongly; 2 = disagree; 3 = agree; 4 = agree strongly.

	DS	D	A	AS
1. A small bribe to make a sale is entirely reasonable.	1	2	3	4
2. As the manager, I would have no problem in taking credit for an innovative idea of a subordinate.	1	2	3	4
3. Supplying a customer with a prostitute to help win a big contract is justified.	1	2	3	4
4. I would be willing to use a video surveillance camera to see what my subordinates are doing when I am out of the office.	1	2	3	4
5. Cheating on your expense account up to about 10 percent of the total expenses is usually justifiable.	1	2	3	4
6. Honest guys and gals tend to finish last.	1	2	3	4
7. If I were fired, I would be willing to get revenge on my employer by taking away trade secrets.	1	2	3	4
8. I would avoid hiring someone into the work group who might become a competitor for my position.	1	2	3	4
9. Overcharging a government customer for goods or services is justified because most companies already pay too much in taxes.	1	2	3	4
10. All things being equal, I would give higher performance evaluations to people of my own ethnic group or race.	1	2	3	4
11. I deliberately give lower performance evaluations to subordinates who I dislike personally.	1	2	3	4
12. I typically play favorites within the group or team.	1	2	3	4
13. I am willing to fake productivity figures just to look good to upper management.	1	2	3	4
14. I would not take time from writing an important report to coach a group member who needed help at the moment.	1	2	3	4
15. I exaggerate the mistakes a subordinate might make just so he or she does not become too self-confident.	1	2	3	4
16. I look for ways to get revenge on any group member who makes me look bad.	1	2	3	4
17. I rarely praise an employee without also finding a way to criticize something he or she has done.	1	2	3	4
18. If a subordinate wants me to do something I do not want to do, I blame upper management for not letting me do it.	1	2	3	4
19. I think it is justified to ask group members to run errands for me, such as getting my car repaired or shopping.	1	2	3	4
20. I will ignore an employee's request to help him or her with a problem just so I can spend some personal time on the Internet.	1	2	3	4

QUIZ 6-1 (continued)

Scoring and Interpretation: Add up your responses to the twenty statements. Recognize that people tend to perceive themselves as more ethical and honest than they really are, so your score could be positively biased.

- **20–25:** If you scored in this range, your self-image is that of a highly ethical and trustworthy leader or potential leader. Assuming that your answers are accurate, your ethics could be an asset to you as a leader.
- **26–45:** Scores in this range suggest the self-image of a leader or potential leader with an average level of ethics. There are probably times when you could behave more ethically.
- **46–80:** Scores in this range suggest the self-image of a highly unethical leader or potential leader. If your score is an accurate reflection of your behavior, you are (or would be) perceived as highly unethical and deviant to the point that it could damage your career. You should study ethics seriously.

Four Ethical Leadership Behaviors

Be Honest and Trustworthy and Have Integrity in Dealing with Others Continuing reports of frauds and scandals in recent years have placed ethical behavior high on the priority list of many organizations. The problem is that ethical problems erode the trust of both leaders and organizations.⁴ Despite the importance of leaders who are trustworthy, evidence suggests that business firms have many ethical problems. As part of an ongoing study of employee attitudes and opinions, the Ethics Resource Center surveyed 2,100 employees among Fortune 500 companies. More than one-half of the respondents observed misconduct, and 28 percent of the employees believed there was no investigation of the misconduct. Another problem was that 22 percent of employees who reported misconduct said they were retaliated against. Thirty-four percent of employees surveyed said that their manager does not display ethical behavior. Also of note, more than 10 percent of employees reported incidences of sexual harassment, stealing, and health and safety violations.⁵

An ethical leader is honest and trustworthy and therefore has integrity. According to ethics researcher Thomas E. Becker, this quality goes beyond honesty and conscientiousness. **Integrity** refers to loyalty to rational principles; it means practicing what one preaches regardless of emotional or social pressure.⁶ For example, a leader with integrity would believe that employees should be treated fairly, and the pressure to cut costs would not prompt him or her to renege on a commitment to reimburse an employee for relocation expenses. As another example, a leader who preaches cultural diversity would assemble a diverse team.

Pay Attention to All Stakeholders Ethical and moral leaders strive to treat fairly all interested parties affected by their decisions. To do otherwise creates winners and losers after many decisions are made. The widely held belief that a CEO's primary responsibility is to maximize shareholder wealth conflicts with the principle of paying attention to all stakeholders. A team of

management scholars observes, “We used to recognize corporations as both economic and social institutions—as organizations that were designed to serve a balanced set of stakeholders, not just the narrow interests of the shareholder.”⁷ A leader interested in maximizing shareholder wealth might attempt to cut costs and increase profits in such ways as (1) laying off valuable employees to reduce payroll costs, (2) overstating profits to impress investors, (3) overcharging customers, and (4) reducing health benefits for retirees. Although these practices may be standard, they all violate the rights of stakeholders.

Jim Goodnight, the CEO of software company SAS, is among the business leaders who contend that there is a strong link between employee satisfaction and increased productivity and profits. He explains, “Because we put employee-oriented measures in place long ago, we have the benefit of years of experience to show that the long-term benefits far outweigh the short-term costs. Most companies don’t know how to represent that kind of return in their annual reports.”⁸

Another behavior of *authentic leaders* is to perceive their role to include having an ethical responsibility to all of their shareholders. The welfare of others takes precedence over their own personal welfare (as in servant leadership). Authentic leaders have a deep commitment to their personal growth as well as to the growth of other stakeholders.⁹

Build Community A corollary of taking into account the needs of all stakeholders is that the leader helps people achieve a common goal. Leadership researcher Peter G. Northouse explains that leaders need to take into account their own and their followers’ purposes and search for goals that are compatible to all.¹⁰ When many people work toward the same constructive goal, they build a community. A business leader who works with many people to help poor schoolchildren is an ideal example of someone who builds a community.

Respect the Individual Respecting individuals is a principle of ethical and moral leadership that incorporates other aspects of morality. If you tell the truth, you respect others well enough to be honest. If you keep promises, you also show respect. And if you treat others fairly, you show respect.¹¹ Showing respect for the individual also means that you recognize that everybody has some inner worth and should be treated with courtesy and kindness. An office supervisor demonstrated respect in front of his department when he asked a custodian who entered the office, “What can we do in this department to make your job easier?”

Factors Contributing to Ethical Differences

There are many reasons for differences in ethics and morality among leaders. Here we look at a variety of these factors.

1. Leader moral identity. A set of studies confirmed the idea that a leader’s *moral identity* has a major influence on his or her level of ethical behavior. A moral identity involves a self-perception organized around a set of moral

traits such as honesty, caring, and compassion. The moral identity acts as a self-regulatory mechanism rooted in a person's sense of what is right and wrong. The studies in question concluded that leaders set the ethical tone of an organization and are instrumental in encouraging ethical behavior among subordinates, as well as reducing interpersonal conflict. Leaders with a strong moral identity are more likely to achieve such good results.¹²

2. Greed, gluttony, and avarice. Many people seek to maximize personal returns, even at the expense of others. Former Federal Reserve chairman Alan Greenspan commented publicly on the problem of executive greed. He said that an infectious greed had contaminated the business community in the late 1990s, as one executive after another manipulated earnings or resorted to fraudulent accounting to capitalize on soaring stock prices.¹³ The devastating stock market downturn in 2008 appeared to have a few similar causes.

Exceptionally high executive compensation could be interpreted as signs of greed and avarice. Two examples are the recent total one-year compensation paid to David Simon of the Simon Property Group (\$137.2 million) and Lawrence Ellison of Oracle (\$96.2 million).¹⁴ Instead of taking so much money for themselves, how about sharing more of the money with employees and stockholders, and offering lower prices for customers? The counterargument is that supply and demand rules, with a limited supply of capable CEOs. So you have to pay talented executives loads of money to stay competitive, even if the compensation exceeds \$100 million per year. Also, an effective CEO can point the firm in the right direction to enhance its prosperity and survival.

3. Rationalization and implied permission. Timothy P. Flynn, chairman of the global accounting firm KPMG, has identified reasons why good people choose the wrong path. One reason is rationalization, which leads people to focus on the intent of the action rather than on the action itself. For example, people might say that they are doing something wrong (such as exaggerating profits) in order to help a client or that they are boosting the stock price to help investors. Another reason is implied permission—"Nobody is telling me to stop, so it must be OK."¹⁵ For example, managers might continue to place only personal friends and relatives in key jobs because they were not told to stop.

4. Moral development level. A notable contributor to a leader's ethics and morality is his or her *level of moral development*. Some leaders are morally advanced, whereas others are morally challenged—a mental condition that often develops early in life. People progress through three developmental levels in their moral reasoning. At the *preconventional level*, a person is concerned primarily with receiving external rewards and avoiding punishment. A leader at this level of development might falsify earnings statements for the primary purpose of gaining a large bonus. At the *conventional level*, people learn to conform to the expectations of good behavior as defined by key people in their environment and societal norms. A leader at this level might be moral enough just to look good, such as being fair with salary increases and encouraging contributions to the United Way campaign. At the *post-conventional*

level, people are guided by an internalized set of universal principles that may even transcend the laws of a particular society. A leader at the post-conventional level of moral behavior would be concerned with doing the most good for the most people, without regard for whether such behavior brought him or her recognition and fortune.¹⁶ The servant leader described in Chapter 4 would be at this advanced level of moral development.

5. Sense of entitlement. The moral excesses of business leaders can occur because many of them have developed a sense of **entitlement**. In the opinion of several psychiatrists and corporate governance experts, some CEOs lose their sense of reality and feel entitled to whatever they can get away with or steal. For example, when John Thain was appointed CEO of Merrill Lynch, he felt entitled to have the company pay \$1.2 million to remodel his office.¹⁷ (Thain lasted less than one year at the Merrill Lynch, partially over disputes about his level of compensation.) Many executives feel entitled to extraordinary compensation. The average CEO pay at major corporations for Standards & Poor's 500 corporations is 204 times that of the average rank-and-file worker; the average of the top 100 companies is 495.¹⁸

6. Situational influences. Unethical and immoral leadership behavior can also be influenced by the *situation*, particularly the organizational culture. If leaders at the top of the organization take imprudent, quasi-legal risks, other leaders throughout the firm might be prompted to behave similarly. The imprudent risks in subprime mortgages taken with investor money by investment banks in recent history might also reflect an aggressive culture. Financial executives were pushed to maximize profits, sometimes not taking into account investor welfare.¹⁹ Many financial specialists believe that the federal government push for availability of mortgages to applicants with low credit ratings encouraged the availability of subprime mortgages to be invested.

7. Character of the person. A person's *character* contributes heavily to ethical differences. The higher the quality of a person's character, the more likely he or she will behave ethically and morally. For example, a leader who is honest and cooperative will tend to behave more ethically than a leader who is dishonest and uncooperative. A person's character is quite close in meaning to moral identity, discussed first in this list. Leadership Self-Assessment Quiz 6-2 digs into the behavioral specifics of good character as perceived by the U.S. Air Force.

8. Motivated blindness. A final factor to be considered here that contributes to unethical leadership behavior is *motivated blindness*, or seeing what we want to see and missing contradictory information. The result can be a conflict of interest, such as a compensation consultant being paid by the CEO to make recommendations about her financial compensation. Although the consultant is attempting to be honest, the desire to please the CEO leads him to recommend a pay package so generous that the CEO becomes overpaid. Another example of motivated blindness is that a manager who hires an individual may not notice the new hire's unethical behavior because the behavior would reflect an error in selecting the new hire.²⁰



LEADERSHIP SELF-ASSESSMENT QUIZ 6-2

The Air Force Character Attributes Checklist

Instructions: Listed and defined next are character attributes the U.S. Air Force wants to see among the ranks of its leaders. For each attribute, note your standing as being high (H), average (A), or low (L). A checklist of this nature lends itself to self-serving bias, so work extra hard to be objective. When applicable, visualize an example of how you have exhibited, or have not exhibited, a particular character attribute.

FACTOR	DESCRIPTION	MY STANDING		
		H	A	L
Integrity	Consistently adhering to a moral or ethical code or standard. A person who consistently chooses to do the right thing when faced with alternative choices.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Honesty	Consistently being truthful with others.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Loyalty	Being devoted and committed to one's organization, supervisors, coworkers, and subordinates.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Selflessness	Genuine concern about the welfare of others and a willingness to sacrifice one's personal interests for others and the organization.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Compassion	Concern for the suffering or welfare of others and providing aid or showing mercy for others.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Competency	Capable of excelling at all tasks assigned. Is effective and efficient.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Respectfulness	Shows esteem for and consideration and appreciation of other people.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Fairness	Treats everyone in an equitable, impartial, and just manner.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Responsibility and self-discipline	Can be depended on to make rational and logical decisions and to do tasks assigned. Can perform tasks assigned without supervision.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Decisiveness	Capable of making logical and effective decisions in a timely manner. Makes good decisions promptly after considering data appropriate to the decision.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Spiritual appreciation	Values the spiritual diversity among individuals with different backgrounds and cultures and respects all individuals' rights to differ from others in their beliefs.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Cooperativeness	Willing to work or act together with others in accomplishing a task toward a common end or purpose.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Interpretation: The more of the attributes you rated as *high*, the more likely it is that others perceive you as having a good character. The list may provide some clues to leadership development. For example, if you are perceived to be low on integrity and cooperativeness, you are less likely to be able to influence others.

Note: Although competency and decisiveness are not ordinarily considered character traits, being competent and decisive contributes to having good character.

Source: U.S. Air Force, as reprinted in Cassie B. Barlow, Mark Jordan, and William H. Hendrix, "Character Assessment: An Examination of Leadership Levels," *Journal of Business and Psychology*, Summer 2003, p. 568.

The Ethical Mind for Leaders

Cognitive and educational psychologist Howard Gardner believes that for a leader to stay ethical, he or she must develop an **ethical mind**, or a point of view that helps the individual aspire to good work that matters to their colleagues, companies, and society in general.²¹ Developing an ethical mind begins with the belief that retaining an ethical compass is essential to the health of the organization. Early life influences, such as encouragement not to cheat on exams or plagiarize when writing papers, are a good start. Next, the leader must state his or her ethical beliefs and stick to them. (The ethical beliefs already mentioned in this chapter are relevant, such as being convinced that attention must be paid to all stakeholders.) The leader must also make a rigorous self-test to make sure values are being adhered to, such as checking to see if merit instead of favoritism is a key criterion for promotion. Taking the time to reflect on beliefs can help the leader stay focused on ethical behavior. Asking mentors to comment on the ethics of your behavior can be a useful reality check. Finally, to stay ethical, the leader should act quickly on strongly unethical behavior of others, such as confronting a colleague who is using the corporate jet for a family vacation.

So which leader has an ethical mind? You will probably find many of them as hard-working middle managers. A famous business leader with an ethical mind might be Sheryl Sandberg based on her high reputation to date. We never know, however, when a business leader with an outstanding reputation for ethical behavior will have a moral lapse at some point.

A review of the literature about ethical leadership behavior reveals dimensions of ethical behavior that help pinpoint more specifically what constitutes an ethical mind. The researchers identified five dimensions of ethical leadership behavior, as described next.²² You will observe that these dimensions support information in this chapter as well as other places in this book.

1. *Fairness.* The leader who practices fairness avoids favoritism, treats others in a manner that is right and equal, and makes principled choices.
2. *Power sharing.* The leader who shares power allows for group member input into decisions and listens to their suggestions, ideas, and concerns.
3. *Role clarification.* To give group members more structure in their work, the leader clarifies responsibilities, expectations, and performance goals.
4. *People orientation.* The leader with people orientation cares about, respects, and supports followers.
5. *Integrity.* A leader with integrity shows a consistency between word and deeds, and keeps promises.

6. *Ethical guidance.* A leader provides ethical guidance by communicating about ethics, explains ethical rules, and encourages and rewards ethical conduct.
7. *Concern for sustainability.* A leader with a true concern for sustainability cares about the environment in such ways as being a champion of recycling.

Guidelines for Evaluating the Ethics of a Decision

Several guidelines, or ethical screens, have been developed to help leaders or other influence agents decide whether a given act is ethical or unethical. The Center for Business Ethics at Bentley College has developed six questions to evaluate the ethics of a specific decision:²³

- *Is it right?* This question is based on the deontological theory of ethics that states there are certainly universally accepted guiding principles of rightness and wrongness, such as “thou shalt not steal.”
- *Is it fair?* This question is based on the deontological theory of justice that certain actions are inherently just or unjust. For example, it is unjust to fire a high-performing employee to make room for a less competent person who is a relative by marriage.
- *Who gets hurt?* This question is based on the utilitarian notion of attempting to do the greatest good for the greatest number of people.
- *Would you be comfortable if the details of your decision or actions were made public in the media or through e-mail?* This question is based on the universalist principle of disclosure.
- *What would you tell your child, sibling, or young relative to do?* This question is based on the deontological principle of reversibility, which evaluates the ethics of a decision by reversing the decision maker.
- *How does it smell?* This question is based on a person’s intuition and common sense. For example, counting a product inquiry over the Internet as a sale would smell bad to a sensible person.

Ethical issues that require a run through the guide are usually subtle rather than blatant, or a decision that falls into the gray zone. An example took place several years ago when GM and Ford offered to buy out the pensions of 140,000 employees, meaning that workers were offered a lump-sum payout instead of monthly payments for the rest of their lives. For example, an employee with 40 years of service might be offered \$500,000, and then receive no more pension money from the company. Employees who refused the buyout would find their plan shifted to a private financial services firm. The ethics of this pension buyout plan might fall into the gray zone because the workers who accept the offer are receiving a large sum of money.²⁴ If these same workers die early, their beneficiaries will have



LEADERSHIP SKILL-BUILDING EXERCISE 6-1

Should “Dinosaur Power” Be Placed on the Market?

A manufacturer of niche beverages such as vitamin water, canned tea drinks, and multi-vegetable bottled drinks, is looking to expand its product line in order to raise revenue. The product development team has been working for several months on an energy-boosting drink, called Dinosaur Power. Product development head Cliff explained to company leadership that energy drinks are among the fastest-growing products in the beverage sector. He pointed out that Dinosaur Power will differentiate itself from the many other products on the market because it will contain an extra-heavy dose of caffeine, will resemble the taste of an alcoholic beverage, and will have a thick cherry taste known to be

habit forming, particularly with young adults. Cliff said, “Our test results show that the energy surge provided by this drink will keep people coming back for more. Consumers will be using it on and off the job to feel energized.”

With company revenues showing signs of declines, sales could use a quick boost, yet there is some concern about releasing what would be the highest-power, and most habit-forming energy drink on the market. Work in a small group to take the contemplated decision about releasing Dinosaur Power into the market through the guidelines for evaluating the ethics of a decision.

profited handsomely. Also, the financial services firm would still provide them with at least a limited pension. Yet, most workers who accept the buy-out will receive much less money than if they received monthly payments for the rest of their life.

Leaders regularly face the necessity of running a contemplated decision through an ethics test. Leadership Skill-Building Exercise 6-1 provides an opportunity to think through the ethics of a decision facing a beverage manufacturer.

A Sampling of Unethical Leadership Behaviors

We have been alluding to unethical behavior in this and previous chapters. Here, we present a sampling of unethical behaviors from the past and present. A statement often made is that about 95 percent of business leaders are ethical and that the 5 percent of bad apples (mostly senior executives) get all the publicity. However, the impact of unethical leadership has been enormous. Unethical behavior has thrown companies into bankruptcy, led to the layoffs of thousands of workers, diminished trust in stock investments, and discouraged many talented young people from embarking on a business career. Table 6-1 presents some unethical, immoral, and often illegal behaviors engaged in by business leaders whose acts have been publicly reported. All of these unethical acts resulted in convictions or indictments rather than simply accusations or allegations. Thousands of other unethical acts go unreported, such as a business owner who places a family member, friend, or lover on the payroll at an inflated salary for work of limited value to the firm.

TABLE 6-1 Examples of Unethical Behavior by Business Leaders.

The sampling of behaviors presented here includes behaviors that resulted in criminal prosecutions, and those that result in only embarrassment and negative press.

LEADER AND COMPANY	OFFENSE AND OUTCOME
Bernard L. Madoff, former CEO of Bernard L. Madoff Investment Securities and also former chairman of Nasdaq (the stock exchange)	<p>Convicted of defrauding investors out of about \$17 billion over a period of years. Basically sold investors phantom investments, pocketed most of the money, and made some payments to new investors from money paid by earlier investors. Had worldwide network of brokers and other contacts sending him referrals. Sent to prison for 150 years for crimes including securities fraud, international money laundering, mail fraud, and wire fraud. At the time of conviction, said he was sorry.</p> <p>The Madoff finance chief, Frank DiPascali, pleaded guilty to 10 counts of conspiracy, fraud, and other charges and faced a 125-year prison sentence. In hopes of gaining leniency, he testified against five former coworkers accused of participating in the fraud.</p>
Angelo R. Mozilo, former CEO of Countrywide Financial (now a unit of Bank of America)	<p>As CEO, played a major role in issuing mortgages to high-risk customers, then sold securities based on these mortgages, touting them as high-rated safe securities. Accused of knowing that many borrowers could not pay back their loans. Paid \$67.5 million in penalties to settle civil fraud and insider-trading charges, but was not prosecuted. Later included as defendant in lawsuit by Allstate Corp., claiming that lax underwriting standards led to collapse of residential mortgage-based securities.</p>
Deon Anderson, former Boeing procurement officer	<p>Anderson and three other executives were indicted by a federal grand jury and accused of engaging in a bribery and kickback scheme. He was accused of leaking nonpublic information to bidders for contracts on military aircraft parts in exchange for cash. Faced a wire fraud count that carries a maximum prison sentence of 20 years, and a 250,000 fine.</p>
Paul Shinn Devine, Global Supply Manager at Apple Inc.	<p>Accused in 2010 by a federal grand jury indictment of receiving more than \$1 million in kickbacks from Apple suppliers in Asia. Devine was charged with offenses including wire fraud, money laundering, and unlawful monetary transactions. Apple also named Devine in a civil suit, with the company saying that it has zero tolerance for dishonest behavior.</p>

Source: The facts in the table have been widely circulated in the media. Representative sources for the facts include the following: Kevin McCoy, "Madoff's Top Aide to Testify Today," *USA Today Money*, December 2, 2013, p. 5B; Roger Parloff, "As If a Credit Tsunami Weren't Enough: The Case of Accused Ponzi Schemer Bernard L. Madoff," *Fortune*, January 19, 2009, p. 61; David Benoit, "Allstate Sues Countrywide," *The Wall Street Journal*, December 29, 2010, p. C2; Shayndi Raice, "Ex-Countrywide Official on Defense," *The Wall Street Journal*, October 16, 2013, p. C3; "Former Boeing Executive, Three Others Indicted in Bribery Scheme," *Bloomberg News*, October 18, 2013; Yukari Iwatani Kane, "For Apple Suppliers, Pressure to Win," *The Wall Street Journal*, August 16, 2010, p. B3; "Executives on Trial," *The Wall Street Journal*, May 26, 2006, p. A9.

Leadership, Social Responsibility, and Creating an Ethical Organizational Culture

The idea of **corporate social responsibility** continues to evolve. One new framework is that such responsibility is part of external engagement, or the efforts a company makes to manage its relationship with the external world. The external engagement should be integrated into decision making at every organizational level. The external engagement should include a wide variety of activities including philanthropy, community programs, aspects of product design, and recruiting policy.²⁵ The initiatives to be described in the following pages are examples of both corporate social responsibility and external engagement.

Being socially responsible fits into the Thou Shalt approach, or finding out better ways for leaders to make a positive contribution to society. In contrast, the Thou Shalt Not approach focuses on avoiding the kind of wrongdoing depicted in Table 6-1.²⁶ When corporate social responsibility generates value for shareholders and stakeholders, it is regarded as good business strategy.²⁷

Our focus here is illustrative actions that leaders can take to enhance social responsibility, as well as create an organizational culture that encourages ethical behavior, as outlined in Figure 6-1.

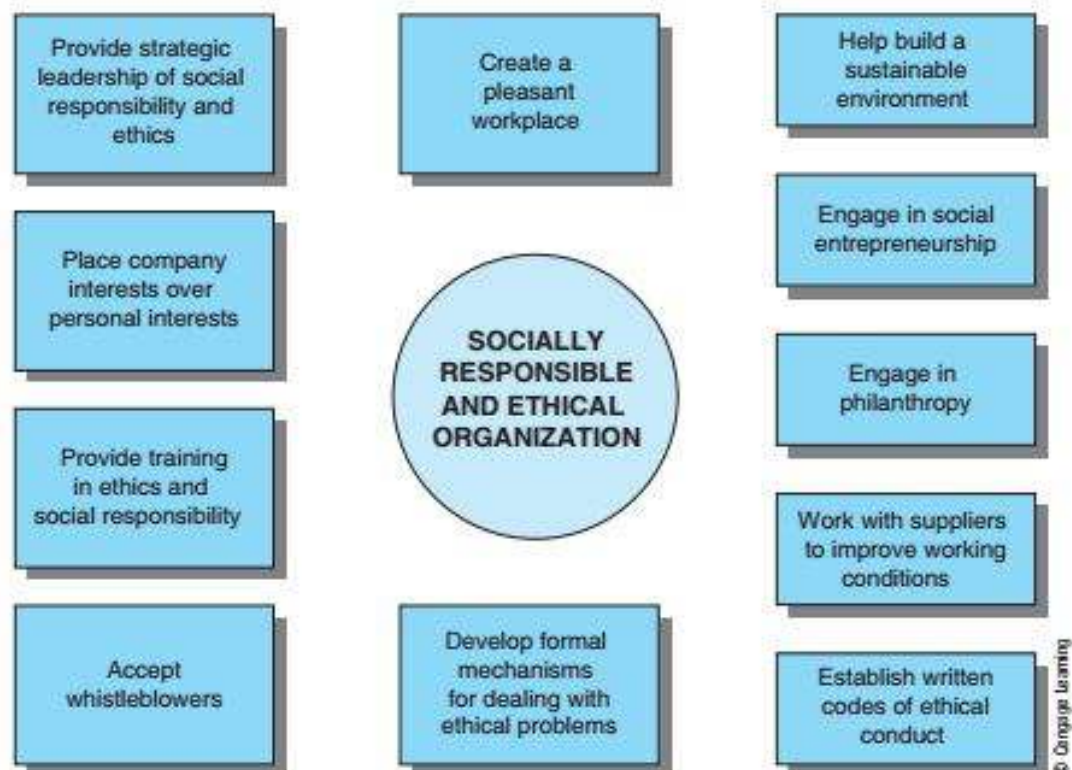


FIGURE 6-1 Initiatives for Achieving a Socially Responsible and Ethical Organization.

Providing Strategic Leadership of Ethics and Social Responsibility

The most effective route to an ethical and socially responsible organization is for senior management to provide strategic leadership in that direction. In this way, senior managers become ethics leaders: Their policies and actions set the ethical and social responsibility tone for the organization. If high ethics receive top priority, workers at all levels are more likely to behave ethically. Around 2008, an analysis of the troubles facing the banking industry suggested that lack of moral leadership was a contributing factor. Christina Rexrode, who follows the banking industry, wrote:

Although the industry faces sweeping new rules and regulations imposed by Congress, legality isn't the same thing as morality. In some corridors of banking, people turned a blind eye to troubling practices—such as the issuance of subprime mortgages—as long as they were technically legal.²⁸

Strategic leadership of ethics and social responsibility includes leading by example. If workers throughout the firm believe that behaving ethically is in and behaving unethically is out, ethical behavior will prevail. Ethical behavior that is rewarded is likely to endure. In addition, workers who perform unethically should not be rewarded, and perhaps disciplined. A sales manager who uses a 35-day month might not be rewarded for sales booked during those five days borrowed from the next month just to look good in the previous months.

Creating a Pleasant Workplace

Creating a comfortable, pleasant, and intellectually stimulating work environment is a social responsibility initiative that directly affects employees' well-being. Because many people invest about one-third of their time at work, a pleasant work environment increases the chances that their lives will be enriched. Robert Levering and Milton Moskowitz of the Great Place to Work[®] Institute, in cooperation with *Fortune*, have institutionalized the idea of being a "best company to work for." Employers nominate themselves, and two-thirds of the score is based on how randomly selected employees respond to the Great Place to Work Trust Index,[®] a survey measuring organizational culture. An evaluation of the Culture Audit by staff members at the Great Place to Work Institute determines the rest of the score. The focus is on employee satisfaction, yet the firms that fall into "the 100 best companies to work for" are also typically profitable. Among the benefits these companies offer are flexible working hours; on-site day care; concierge services, such as dry-cleaning pickup; domestic-partner benefits to same-sex couples; and fully paid sabbaticals. Following are the three of the most highly rated companies:²⁹

Google, Mountain View, California: The business firm whose name has become a verb sets the standard for Silicon Valley. Google has placed first four times so far as a *Fortune* best company to work for. Among its perks are free gourmet meals, free

massages, a seven-acre sports complex, and free medical services on-site. Engineers are empowered to spend 20 percent of their time on independent projects. Google employees are empowered to award one another \$175 on-the-spot peer spot bonuses, and more than two-thirds of “Googlers” made the awards. Hiring standards are tough, emphasizing brilliance, good team player skills, and diverse interests.

SAS, Cary, N.C.: This business analytics software and services firm took the top spot among Best Companies for two consecutive years and has been on the list for sixteen years. Notable perks include on-site health care (also available to family members), summer camp for employee children, organic farm-produced food for the four company cafeterias, car wash and interior cleaning service, a salon, and a massive gym on company premises. The company philosophy is “Treat employees like they make a difference and they will.”

Carmax, Richmond, Virginia: This nationwide dealership operates 117 no-haggle used-car lots. Floor employees wear uniforms, and the stores are family friendly. Sales reps are salaried to help motivate them to do what is best for the customer. Associates are authorized to take off as much time as they need without an established limit. The CEO increases his accessibility to employees by means of town hall meetings and cookouts.

The employee programs that qualify a company as a best place to work focus on employee benefits. However, the leaders of these companies also emphasize stimulating work.

Helping Build a Sustainable Environment

Socially responsible leaders influence others to sustain and preserve the external environment through a variety of actions that go beyond mandatory environmental controls such as managing toxic waste. Helping build a sustainable environment can involve hundreds of different actions such as making packaging smaller; making more extensive use of fluorescent lighting; and, when feasible, using energy from solar panels and wind turbines to replace burning of fossil fuels. Furthermore, many companies sponsor team-building events, in which participants build a playground or refurbish an old house in a declining neighborhood. Preserving an old building uses less energy than constructing a new one, and it enhances the aesthetics of the environment, as well.

A relatively new leadership position has been created in several firms, bearing a title such as chief sustainability officer. At Coca-Cola Co., the major role of chief sustainability officer Beatriz Perez is to work on sustainability issues in packaging and recycling, water, climate protection, and community.³⁰ At Nike Corporation, Hannah Jones is vice president of sustainable business & innovation. She is responsible for stewarding Nike’s global sustainability and labor rights strategies.³¹

Three specific examples of representative leadership initiatives for helping create a sustainable environment follow:

- Pioneer Millworks, a small business of 105 employees, takes old items destined for landfills, or left to rot, and transforms them into beautiful

objects. For example, wine barrels made from redwood, Cyprus, and Douglas fir, are dismantled and processed. The revitalized wood is then used for flooring or paneling in upscale homes and restaurants, and hip office places. All of the company's electricity is either bought from wind and power sources or generated from solar panels. Scrap wood from cutting and shaping is used as fuels in kilns or to heat the workplace.³²

- Levi-Strauss & Co., manufactures a line of jeans called Waste<Less™ that incorporates an average of eight 12- to 20-ounce recycled plastic bottles per pair of jeans. Plastic bottles are converted into polyester fabric and blended with cotton. The payoff to the environment is that fewer plastic bottles wind up in landfills, and less new material is required to make the jeans.³³
- UPS has improved the fuel efficiency of its domestic delivery fleet by 10 percent in recent years. To improve another 10 percent, the company has added more alternative fuel vehicles. UPS now has all-electric vehicles, hybrid-electric vehicles, vehicles that run on compressed natural gas, and those that run on liquid natural gas.³⁴ A newer development is the use of trucks with plastic rather than aluminum paneling, creating a lighter, more fuel-efficient vehicle.

In addition to gaining favorable publicity for the company, the environment benefits from the type of initiatives just described. Another way for a leader to help the environment is to be in the recycling business. Electronic recycling is particularly important because electronics are the fastest-growing solid waste stream in the world and contain toxins such as mercury and chromium. A sizable company in this field is Electronic Recyclers International in Fresno, California. The business has been increasing by approximately 50 percent per year. ERI chief executive John S. Shegerian takes performing a good deed for society one step further: One-third of the 200 full- and part-time employees are part of its second chance program, which includes primarily ex-cons and former addicts.³⁵ The social-good aspect is that being employed facilitates a person's not lapsing back into criminal behavior and drug addiction.

For company leadership to better evaluate their sustainability initiatives, it is important to rigorously evaluate the steps, the processes they are using, and the true impact on the environment. According to the research of Magali A. Delmas, Dror Etzion, and Nicholas Nairn-Birch, 80 percent of corporate environmental performance is accounted for by two factors. One is the environmental processes and practices implemented by the firm; and the other is the environmental outcomes they generate.³⁶

A case in point is the Waste<Less denim collection of Levi-Strauss. In one year, 3.5 million recycled plastic bottles are used in the spring collection—an admirable process. Yet, the true impact on the environment would be how many plastic bottles are really removed from the environment. If landfills and waters became less clogged, the environmental impact would be substantial. However, if these same plastic bottles would have been converted to other uses anyway, such as plastic benches, driveways, and ball-point pens, the environmental impact would be zero.

The accompanying Leader in Action describes the efforts of two well-known consumer products companies in creating a more sustainable



LEADER IN ACTION

Leadership at Coca-Cola and Nestlé Waters Protects Freshwater Supplies

Former U.S. Attorney John Ashcroft said during a conference at the Wharton School that “if water runs out, it will be more important than if the oil runs out. Corporate leaders can redefine the possible in these areas. When companies take initiative with intensity and enthusiasm, they can actually lead the customer.”

Coca-Cola and Nestlé Waters are two companies that focus on protecting the world’s increasingly challenged freshwater supplies. Coca Cola noted in a sustainability report that because it sells its products where it makes them, the company added to “the ecological and ethical imperatives that drive our water stewardship, we also have a vested business interest in preserving and improving local water sources.”

Jeff Seabright, vice president of environmental and water resources at Coca-Cola, noted at the conference that water and agricultural production are tightly intertwined. Succeeding at transforming company-wide operations will take more than a board vote. Seabright pointed out that Coca-Cola follows a franchise model, so it must work with 200 other companies, 500 brands, 300 independent bottling partners, and 1,000 manufacturing facilities.

Among its goals, Coca-Cola aims to increase waste efficiency 25 percent by 2020, and that same year “safely return to communities and nature an amount of water equal to what we use in our finished beverages and their production.” It wants to be a “net-zero” user of water.

Coca-Cola has also committed \$30 million over six years to the Replenish Africa Initiative (RAIN), which will give two million people access to safe drinking water by 2015. RAIN intends to start more than 100 water access programs in Africa.

Some 40 percent of Nestlé Global’s factories are in regions experiencing water stress, and 10 percent are in areas of severe scarcity. The company is reducing its water withdrawal (in part through rainwater harvesting), at the same time it increases operating efficiency. In the long run, the efficiencies “reduce operating costs and conserve scarce resources,” says Michael Washburn, vice president of sustainability at Nestlé Waters in North America. “Yes, our projects have to pay back in a certain amount of time, but our company gives us flexibility on taking a longer time to pay back.”

Bottled water, meanwhile, has its own imperatives. “We produce a product that in certain quarters is controversial, and has a precise set of societal expectations,” said Washburn. “We’re expected to be good stewards, to be involved in responsible disposal of our packaging, and to use energy as efficiently as possible. If we fall short on any of those things, we’re confronted with a societal backlash.”

Sustainability, said Washburn, in some cases provokes engagement outside the company’s own boundaries. In north Florida, Nestlé works with the Suwanee River Partnership to help farmers with best practices in irrigation, and use of fertilizers and herbicides, to reduce effluent releases into rivers and streams. Also in Florida, the company is working with Southern Forestry Consultants to manage its 468-acre certified tree farm for optimal soil conservation and biodiversity.

Because Nestlé Waters draws its product from springs, not rivers, why do that work with ranchers? “It’s about local relationships,” said Washburn. We are present in twenty-six communities around the country where we have factories, and our employees live there and interact with stakeholders there. We actively seek positive community engagement, because it builds brand equity and local trust. It’s not a selfless act, because there are benefits that come back to our company.”

QUESTIONS

1. To what extent should business leaders take positive actions to improve the world’s freshwater supply?
2. To what extent do you think Coca-Cola and Nestlé Waters are simply engaging in a public relations gimmick in their efforts to improve the quality of local water supplies?
3. What specific benefits might come back to Coca-Cola and Nestlé Waters from their investments of resources in producing potable water?
4. Has the information presented about the Coca-Cola and Nestlé companies influenced whether or not you will purchase any of their products?

Source: Excerpted and adapted from “Resource Scarcity Will Recast Corporate Environmental Behavior,” *Knowledge @Wharton* (<http://knowledge.wharton.upenn.edu/>), June 28, 2013, pp. 4–5.



LEADERSHIP SKILL-BUILDING EXERCISE 6-2

Conducting an Environmental Audit

To create an environmentally friendly workplace, somebody has to take the initiative to spot opportunities for change, thereby exercising leadership. Organize the class into groups of about five, with one person being appointed the team leader. You might have to do the work outside of class because your assignment is to do an environmental audit of a workplace that might include nonprofit setting such as a place of worship, a school, or an athletic facility. If the audit is done during class time, evaluate a portion of the school, such as a classroom, an athletic facility, or the cafeteria. Your task is to conduct an environmental audit with respect to the energy efficiency and healthfulness of the workplace. Make judgments, perhaps on a 1-to-10 scale, plus comments about the following factors:

1. How energy efficient is the workplace in terms of such factors as building insulation, use of fluorescent lighting, heating and cooling, and use of solar panels?
2. How safe is the environment in terms of pollutants and steps to prevent physical accidents?
3. How aesthetic is the environment in terms of protecting against sight and sound pollution?

Summarize your findings and suggestions in a bulleted list of less than one page. Present your findings to classmates and perhaps to a manager of the workplace. Classmates might comment on whether your findings will really improve the planet from an ecological standpoint.

environment. Leadership Skill-Building Exercise 6-2 provides an opportunity for you to practice conducting an environmental audit.

Engaging in Social Entrepreneurship

A social responsibility initiative gaining momentum is **social entrepreneurship**, the use of market-based methods to solve social problems.³⁷ Social entrepreneurship is therefore an entrepreneurial approach to social problems such as homelessness, contaminated drinking water, damaged physical environments, and extreme poverty. John S. Shegerian at Electronic Recyclers could therefore be regarded as a social entrepreneur. Leaders at a business firm might also form a foundation to help a cause, or be a socially focused, for-profit company such as Better World Books. Through the sale of used and new books, one of the company's social initiatives is to fund literacy programs around the world. Partners of Better World build schools, launch libraries, and provide scholarships.³⁸

A research-based model of social entrepreneurship emphasizes that compassion encourages social entrepreneurship. Compassion in the model is viewed as a prosocial (helping others) motivation that connects the individual with a suffering community and triggers sensitivity to the pain and needs of others.³⁹ An exceptional example of a business leader with compassion is Father Gregory Boyle, the CEO of Homeboy Industries. The beginning mission of the company was to create jobs for former Los Angeles gang members, many of whom had prison records. The company takes former men and women gang members and trains them in job-related skills, starting with custodial work, followed by baking skills. To create work for the former gang

members, Boyle started a bakery. The product line has expanded into items such as chips and salsa dip. The food product has become so popular in stores that Homeboy recently had 2,500 accounts and growing.⁴⁰

Engaging in Philanthropy

A standard organizational leadership approach to social responsibility is to donate money to charity and various other causes. Most charities are heavily dependent on corporate support. Colleges, universities, and career schools also benefit from corporate donations. Many of the leading philanthropists donate money during their lifetime rather than giving through their estates. The most striking example is Bill and Melinda Gates of Microsoft, who formed their own foundation with the primary global aims of reducing extreme poverty, combating AIDS, and vaccinating children against illnesses. Financier Warren Buffet is also a director of the foundation. In the United States, the focus is more on educational opportunities and access to information technology. In 2014, the foundation had an endowment of over \$45 billion, with Buffet having doubled the endowment in 2006. Furthermore, Bill Gates has called for a revision of capitalism in which poor people receive more benefits. Gates said he is troubled because advances in technology, health care, and education tend to help the rich and neglect the poor.⁴¹

Many corporate donors want their charitable investments to benefit the end consumer, not get lost in red tape and overhead, and show measurable results. The new breed of philanthropist studies each charitable cause as he or she would a potential business investment, seeking maximum return in terms of social impact. This philanthropist might also seek follow-up data, for example, on how many children were taught to read or by what percentage new cases of AIDS declined.

Working with Suppliers to Improve Working Conditions

An opportunity for practicing social responsibility is for company leaders to work with suppliers to improve physical and mental working conditions. Instead of refusing to deal with a supplier who operates a sweatshop, management might work with the supplier to improve plant working conditions. The justification for helping the supplier improve conditions is that the supplier's employees are often in dire need of a paying job. Almost any job is better than no job to a person facing extreme poverty or who is dependent on modest wages for food and shelter. Helping suppliers improve working conditions has been conceptualized as corporations being vehicles for positive social change—yet another way of demonstrating corporate social responsibility.⁴² Another form of helping to improve working conditions is to assist factory management to repair potential hazards such as inadequate escape routes in case of fire.

Apple Inc. is one example whereby company leadership took action to work with suppliers to improve substandard working conditions. Worker advocates and Apple representatives found that workers assembling iPhones, iPads, and other Apple devices often work in harsh and dangerous

conditions. It was found that many employees worked excessive overtime, lived in crowded dorms, and often stood at the assembly tables for such a long time that their legs swelled until they could barely walk. Underage workers were often included in the workforce of subcontractors. In recent years, Apple made significant progress in improving the factories. The company now has a supplier code of conduct that provides specific guidelines on labor standards and safety protection. Apple conducts thorough audits, and when abuses are discovered, corrections are required for the subcontractor to continue to be an Apple supplier.⁴³ Apple leadership has to stay vigilant to labor abuses, because labor abuses have a tendency to resurface, as reported by China Labor Watch, a nonprofit group.

Establishing Written Codes of Ethical Conduct

Many organizations use written codes of conduct as guidelines for ethical and socially responsible behavior. Regardless of the industry, most codes deal with quite similar issues. Patricia Breeding, integrity compliance officer for Covenant Health, in Knoxville, Tennessee, says, “They all address conflicts of interest, gifts and things like vendor relationships. They use the word ‘customer’ in one and ‘patient’ in another but they’re all about doing the right thing.”⁴⁴

Prohibition against bribery of government or corporate officials is being incorporated more frequently into ethical codes to combat potential major problems. For example, in 2011, U.S. regulators accused IBM of ten years of bribery in Asia, contending that employers handed over shopping bags filled with cash in South Korea. IBM allegedly also arranged junkets for government officials in China in exchange for millions of dollars in contracts. IBM agreed to pay \$10 million to settle the civil charges in which more than 100 employees of IBM subsidiaries were involved in the bribes.⁴⁵ (This case is remarkable because IBM has a positive reputation for ethics and social responsibility.)

The Sarbanes–Oxley Act, triggered by the financial scandals around the year 2000, requires public companies to disclose whether they have adopted a code of ethics for senior financial officers. In some firms, workers at all levels are required to sign the code of conduct. At defense contractor Lockheed Martin Corp., the incoming chief executive Christopher Kubasik was dismissed for “having a close personal relationship” with a subordinate. Although not sexual harassment, the relationship violated the company’s code of ethics.⁴⁶ A written code of conduct is more likely to influence behavior when both formal and informal leaders throughout the firm refer to it frequently. Furthermore, adherence to the code must be rewarded, and violation of the code should be punished.

Developing Formal Mechanisms for Dealing with Ethical Problems

Many large employers have ethics programs of various types. Large organizations frequently establish ethics committees to help ensure ethical and socially responsible behavior. Top-level leadership participation in these

formal mechanisms gives them more clout. Committee members include a top management representative, plus other managers throughout the organization. An ethics and social responsibility specialist from the human resources department might also join the group. The committee establishes policies for ethics and social responsibility and may conduct an ethical audit of the firm's activities. In addition, committee members might review complaints about ethical problems.

Company ethics teams often establish an ethics hotline that enables workers who have questions about ethical behavior or want to report an ethics violation speak with a company official. Hotlines of this nature are more likely to be used when employees throughout the organization do not fear retaliation for reporting an ethical violation.

Accepting Whistleblowers

A **whistleblower** is an employee who discloses organizational wrongdoing to parties who can take action. Whistleblowers often go directly to a federal government bureau to report what they consider to be fraud and poor ethics by their employer. One of the largest settlements was \$920 million against Tenet Healthcare Corp., the nation's second-largest hospital chain. Following allegations by six whistleblowers, prosecutors accused Tenet of overbilling the government by \$806 million in Medicare payments and paying \$49 million in kickbacks to physicians who referred patients to the health care organization.⁴⁷

Whistleblowers are often ostracized and humiliated by the companies they hope to improve. For example, they may receive no further promotions or poor performance evaluations. Also, many whistleblowers are fired or demoted, even for high-profile tips that proved true.⁴⁸ The Sarbanes–Oxley Act includes some protection for whistleblowers. Employees who report fraud related to corporate accounting, internal accounting controls, and auditing have a way of gaining reinstatement, as well as back pay and legal expenses. More than half of the pleas of whistleblowers are ignored.

Because the pleas of whistleblowers are often dismissed, it is important for leaders at all levels to create a comfortable climate for legitimate whistleblowing. The leader needs to sort out the difference between a troublemaker and a true whistleblower.

Being a whistleblower requires a small act of leadership, in the sense of taking the initiative to bring about change. However, leaders of the organization that is turned in might not perceive the change as constructive.

Providing Training in Ethics and Social Responsibility

Forms of ethics training include messages about ethics and social responsibility from company leadership, classes on ethics at colleges, and exercises in ethics. These training programs reinforce the idea that ethical and socially responsible behavior is both morally right and good for business. Much of the content of this chapter reflects the type of information communicated in such programs. Training programs in ethics and social responsibility are most likely to be effective when the organizational culture encourages ethical behavior.

Caterpillar, the manufacturer of construction and mining equipment, exemplifies a modern approach to training in ethics. During the annual training, all 95,000 employees ponder a series of questions presented to them either via the Internet or on paper. The scenarios, written in-house, encourage workers to consider the best way to behave in a particular situation. Employees are able to consult the code of ethics as they reflect on the scenarios. One scenario involves a plant-floor employee adding a cleansing agent used by other employees to the agent the employee is presently using. One of the alternatives is “Check with an environmental health and safety group to ensure the combination is safe.”⁴⁹

Leadership Skill-Building Exercise 6-3 gives you the opportunity to engage in a small amount of ethics training.

Placing Company Interests over Personal Interests

Many ethical violations, such as senior managers voting themselves outrageous compensation, stem from managers placing their personal interests over the welfare of the company and other employees. According to the research and theorizing of management professors Craig L. Pearce, Charles C. Manz, and Henry P. Sims Jr., executives are more likely to be less corrupt (and therefore placing company interests first) when leadership is shared. The researchers reason that power can corrupt and absolute power can be an especially toxic influence. Shared leadership can provide a robust system of checks and balances, thereby reducing the possibility of some unethical and criminal behavior by business executives.⁵⁰ Nevertheless, we still have to be realistic. Criminal business leaders such as Bernie Madoff probably enlisted the cooperation of a few other executives (thereby engaging shared leadership) to pull off their massive swindles.

Leadership Skill-Building Exercise 6-3 gives you an opportunity to work through issues of ethics and social responsibility.



LEADERSHIP SKILL-BUILDING EXERCISE 6-3

Getting More Bang for the Buck with Layoffs

Your assignment as mid-level leaders in a large company is to develop a list of workers to lay off for purposes of company downsizing. The CEO says that she wants you to develop a list of fifty employees to lay off. She says that the more money you save the company, the better, but that you should still pay some attention to retaining high-producing workers. As you and your team start poring over employee salaries, you notice that the older employees are often the most highly paid because they have received salary increases for many years. These high-paid workers are a mix of

outstanding, average, and below-average performers based on the results of performance evaluations. You also notice that some of the younger employees who are not necessarily outstanding performers are relatively low paid.

Your job is to develop criteria for choosing fifty employees to lay off, taking into account both financial and ethical factors. You want to practice ethical and socially responsible leadership, but you also want the lay off to save the company a lot of money, thereby keeping your CEO happy.

Ethical and Socially Responsible Behavior and Organizational Performance

High ethics and social responsibility are sometimes related to good financial performance. A model of the relationship between corporate social performance and profits emphasizes the role of supply and demand. The model states that when demand for investments in social responsibility increases, value-maximizing managers will find it in their self-interest to make these investments even if cash flow is reduced. Also, despite spending money, the market value of the firm might increase when the demand for these investment opportunities is greater than the supply. An example might be that investing in programs to improve literacy among poor children might have a payoff because there is a big demand for this type of investment.⁵¹ However, investing money to help preserve reptiles in the Arizona desert might not have a good return because of low demand.

A group of researchers from the Boston Consulting Group and World Economic Forum found that many companies in emerging economies take steps to preserve the environment. Two examples are Florida Ice & Farm in Costa Rica and Shree Cement in India. The study also found that the enterprises pursuing sustainability have consistently above-average growth rates and profit margins. Sustainable practices in these companies include investing at first in more environmentally-friendly operating methods that eventually lead to lower operating costs and higher yields. For example, it might take a lot of money up front to invest in a water-recycling system, but the payoff would be substantial in the long run.⁵²

The relationship between social responsibility and profits can also work in two directions: More profitable firms can better afford to invest in social responsibility initiatives, and these initiatives can lead to more profits. The relationship between social and financial performance may be a **virtuous circle**, meaning that corporate social performance and corporate financial performance feed and reinforce each other.⁵³

According to a study conducted by the Ethics Resource Center, employees who work in an ethical environment tend to be better motivated. The study concluded that the chance to contribute to something larger than themselves and be recognized for it is a strong incentive to employees for delivering superior performance.⁵⁴ Using this approach, it is helpful if company leaders explain why the work is larger than oneself, such as a cement manufacturer explaining to employees that the cement is vital for building infrastructure that serves the needs of many people.

Being ethical also helps avoid the costs of paying huge fines for being unethical. According to the Carnegie Council for Ethics in International Affairs, during an eight-year period Wal-Mart paid about \$1 billion in damages to U.S. employees in six different cases related to unpaid work.⁵⁵ Being accused of unethical and illegal behavior can also result in a sudden drop in customers and clients, as well as extreme difficulty in obtaining new customers and clients.

Another key payoff from high corporate social responsibility is the ability to attract high-quality employees. A nonprofit organization, B Lab, certifies business firms that demonstrate sustainable business practices such as producing less waste, purchasing from local suppliers, compensating employees fairly, and having a clearly stated social mission. Close to 900 firms have received such designation, including Patagonia Inc., (top-quality outdoor clothing), Ben & Jerry's (rich ice cream), and Method Products Inc. (cleaning supplies). Leadership at many B Lab companies claims that the certification has been helpful in recruiting, especially among environmentally-conscious young people.⁵⁶

A study conducted with 1,084 employees from seventeen countries suggests that when workers perceive the employer to have high corporate social responsibility, they tend to be more emotionally committed to the company. Perceptions of corporate social responsibility were measured by responses to statements such as, "Does our company do enough towards protecting the environment," and "How satisfied are you with the way your company is taking responsibility for its employees?" An example of a statement measuring commitment was, "Overall, how strong is your sense of loyalty to the company."⁵⁷ Employee commitment often improves organizational performance because turnover decreases, and workers invest more effort into their jobs.

In short, a leader who is successful at establishing a climate of high ethics and social responsibility can earn and save the company a lot of money. Yet, there are times when being socially responsible can eat into profits. For example, installing solar panels in a geographic area with limited sunshine might create a long payback from the panels.



READER'S ROADMAP

So far in this book, we have examined the nature of leadership; the inner qualities of leaders; and leadership styles, contingency leadership, and the leader's ethical behavior and social responsibility. In the next chapter, we focus on how leaders acquire and maintain power and their use of organizational politics.

SUMMARY

Principles of ethical and moral leadership all center on the idea that a leader should do the right thing, as perceived by a consensus of reasonable people. Key principles of ethical and moral leadership are as follows: (1) be honest and trustworthy and have integrity in dealing with others, (2) pay attention to all stakeholders, (3) build community, and (4) respect the individual.

Differences in ethics and morality can be traced to eight factors: (1) leader moral identity; (2) the

leader's level of greed, gluttony, and avarice; (3) rationalization and implied permission to engage in unethical acts; (4) the leader's level of moral development; (5) a sense of entitlement; (6) situational influences; (7) a person's character; and (8) motivated blindness. It has been proposed that to stay ethical a leader must develop an ethical mind focused on good work.

Before reaching a decision about an issue that is not obviously ethical or blatantly unethical, a leader

or manager should seek answers to questions such as: Is it right? Is it fair? Who gets hurt? Unethical behavior has brought companies into bankruptcy, led to layoffs of thousands of workers, diminished trust in stock investments, and discouraged many talented young people from embarking on a business career.

Another way a leader can be ethical and moral is to spearhead the firm, or a unit within it, toward doing good deeds—toward being socially responsible and creating an ethical organizational culture. Among the many possible socially responsible and ethical acts are (1) providing strategic leadership of social responsibility and ethics, (2) creating a pleasant workplace, (3) helping build a sustainable environment, (4) engaging in social entrepreneurship, (5) engaging in philanthropy, (6) working with suppliers to improve working conditions, (7) establishing written codes of conduct, (8) developing formal

mechanisms for dealing with ethical problems, (9) accepting whistleblowers, (10) providing training in ethics, and (11) placing company interests over personal interests.

High ethics and social responsibility are sometimes related to good financial performance, according to research evidence and opinion. Causes in big demand are more likely to have a financial payoff. More profitable firms have the funds to invest in good social programs. Employees who work in an ethical environment tend to be better motivated. Being ethical helps avoid big fines for being unethical, and ethical organizations attract more employees. Corporate social responsibility can help in recruiting talented employees, and can lead to higher commitment to the company. Socially responsible behavior can be cost-effective. However, being socially responsible can sometimes lower profit margins.

KEY TERMS

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entitlement 184

ethical mind 186

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whistleblower 198

virtuous circle 200



GUIDELINES FOR ACTION AND SKILL DEVELOPMENT

A solid foundation for developing a leadership career is to establish a personal ethical code. An ethical code determines what behavior is right or wrong, good or bad, based on values. The values stem from cultural upbringing, religious teachings, peer influences, and professional or industry standards. A code of professional ethics helps a leader deal with such issues as accepting bribes, backstabbing coworkers, and sexually harassing a work associate.

A provocative explanation of the causes of unethical behavior emphasizes the strength of relationships among people. Assume that two people have close ties to each other—they may have worked together for a long time or have known each other both on and off the job. As a consequence, they are

likely to behave ethically toward one another on the job. In contrast, if a weak relationship exists between two individuals, either party is more likely to treat the other badly. In the work environment, the people involved may be your work associates, your contacts, or your internal and external customers.⁵⁸ The message is for you as a leader to build strong relationships with others in order to increase the frequency of ethical behavior.

Discussion Questions and Activities

1. If reputable companies such as IBM and Apple have been charged with using bribes to obtain sales, why should you worry about being ethical?

2. The majority of business executives accused of unethical behavior have studied ethics either as a subject in a business course or as an entire course. So what do you think went wrong?
3. Suppose you had inside information that your employer was thinking about declaring bankruptcy, and you find out that a family member was about to purchase \$20,000 in the stock of your employer. To what extent would it be unethical for you to dissuade the family member from making the investment?
4. How can consumers use the Internet to help control the ethical behavior of business leaders?
5. What is your position on the ethics of a business leader's receiving \$100 million or more in annual compensation?
6. Should leaders of companies that produce fattening food that can lead to cardiac problems and obesity be targeted for being socially irresponsible?
7. What social responsibility obligations should top-level management of major retailers have for the severe injuries that often take place in their stores on Black Friday? (This is the highly promoted shopping event that takes place after Thanksgiving Thursday)?
8. How fair do you think it is to deny an executive a CEO position he or she had been promised because of a romantic relationship with a subordinate? Explain your reasoning.
9. As a present or future organizational leader, what can you do to be an ethical role model for others?
10. In this chapter, we have discussed ethical problems mostly in business. For sake of fairness and balance, identify a few ethical problems you have observed among lawyers, physicians, politicians, or sports figures.

LEADERSHIP CASE PROBLEM A

Are Drivers or Smartphones to Blame?

Top-level leaders at a company that manufactures smartphones, tablet computers, and portable music players, among other electronic devices held a one-day retreat. The purpose was to think through how well the company was contributing to society. Technology chief, Olivia, commented, "I am very proud of us as a company. Think of what we have done for the world. Because of our products, people are more productive, smarter, and happier. At any time of the day, millions of users can access the information they need, and get in touch with whoever they want. Furthermore, they don't have to clutter their minds with facts, or even know how to spell correctly, or do basic math. With the tap of a few buttons, or touching a screen, they get all the information they need."

CEO Raphael added, "You are so right Olivia. Also, people don't even have to pay for landline telephones any longer. And think of how hundreds of companies can hire fewer people because of our devices. I learned recently that many car dealer-

ships have laid off many of their in-store sales reps because a good deal of car purchasing is now done over the Internet. And people don't have to purchase those ink-laden newspapers because they can get all the information they need on a hand-held device."

Derek, the marketing manager, with a worried look said to the group. "We all make a great living from the electronic devices we make and sell, and so do our competitors. The information technology industry has created millions of jobs. And maybe we have also eliminated millions of jobs. However, I want us as industry leaders to focus on one issue right now.

"The accidents and deaths our devices are facilitating are getting out of hand. At first it was people sending and receiving calls on their cell phones that was creating driving hazards. Then along came texting which is even a bigger problem. Now we have data that the number of people who surf the Internet while driving is surging.