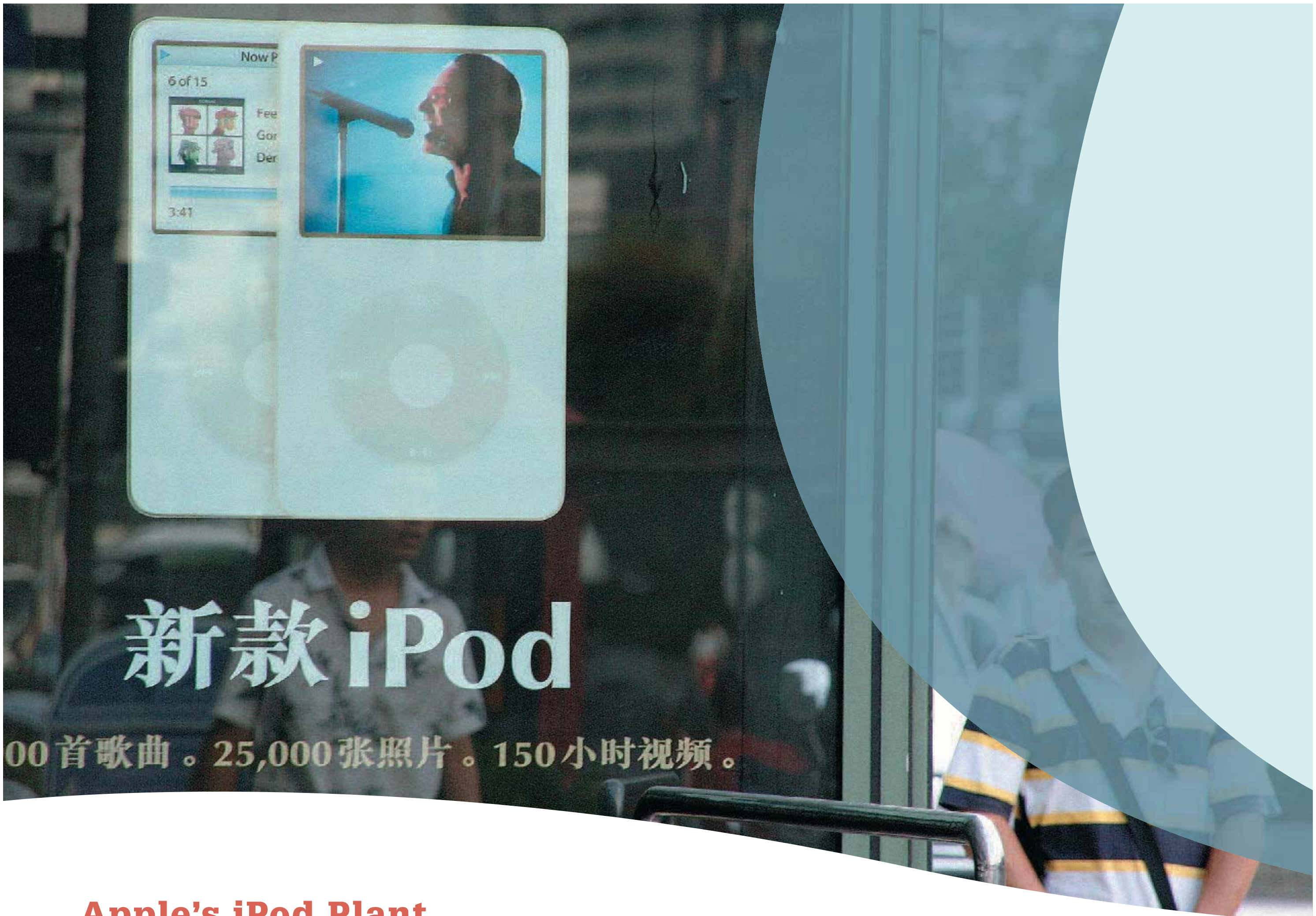


Apple's iPod Plant

In mid-2006 news reports surfaced suggesting that there were systematic labor abuses at the factory in China that makes the iconic iPod for Apple Computer. According to the reports, workers at Hongfujin Precision Industries were paid as little as $50 a month to work 15-hour shifts making the iPod. There were also reports of forced overtime and poor living conditions for the workers, many of whom were young women who had migrated in from the countryside to work at the plant and lived in company-owned dormitories. The articles were the work of two Chinese journalists, Wang You and Weng Bao, employed by China Business News, a state-run newspaper. The target of the reports, Hongfujin Precision Industries, was reportedly China's largest export manufacturer in 2005 with overseas sales totaling $14.5 billion. Hongfujin is owned by Foxconn, a large Taiwanese conglomerate, whose customers in addition to Apple include Intel, Dell Computer, and Sony Corporation. The Hongfujin factory is a small city in its own right, with clinics, recreational facilities, buses, and 13 restaurants that serve the 200,000 employees.

Upon hearing the news, management at Apple responded quickly, pledging to audit the operations to make sure that Hongfujin was complying with Apple's code on labor standards for subcontractors. Managers at Hongfujin took a somewhat different tack—they filed a defamation suit against the two journalists, suing them for $3.8 million in a local court, which promptly froze the journalists' personal assets pending a trial. Clearly, the management of Hongfujin was trying to send a message to the journalist community: criticism would be costly. The suit sent a chill through the Chinese journalist community since Chinese courts have shown a tendency to favor powerful locally based companies in legal proceedings.

Within six weeks, Apple had completed its audit. The company's report suggested that although workers had

Ethics in International Business

4

LEARNING OBJECTIVES:

After you have read this chapter you should:

- LO1 Be familiar with the ethical issues faced by international businesses.
- LO2 Recognize an ethical dilemma.
- LO3 Discuss the causes of unethical behavior by managers.
- LO4 Be familiar with the different philosophical approaches to ethics.
- LO5 Know what managers can do to incorporate ethical considerations into their decision making.

not been forced to work overtime, and were earning at least the local minimum wage, many had worked more than the 60 hours a week that Apple allowed, and their housing was substandard. Under pressure from Apple, management at Hongfujin agreed to bring their practices in line with Apple's code, committing themselves to building new housing for employees and limiting work to 60 hours a week.

However, Hongfujin did not immediately withdraw the defamation suit. In an unusually bold move in a country where censorship is still commonplace, Chinese Business News gave its unconditional backing to Wang and Weng. The Shanghai-based news organization issued a statement arguing that what the two journalists did "was not a violation of any rules, laws or journalistic ethics." The Paris-based group, Reporters Without Borders, also took up the case of Wang and Weng, writing a letter to Apple's CEO Steve Jobs that stated, "We believe that all Wang and Weng did was to report the facts and we condemn Foxconn's reaction. We therefore ask you to intercede on behalf of these two journalists so that their assets are unfrozen and the lawsuit is dropped."

Once again, Apple moved quickly, pressuring Foxconn behind the scenes to drop the suit. In early September, Foxconn agreed to do so and issued a "face saving" statement saying that the two sides had agreed to end the dispute after apologizing to each other "for the disturbances brought to both of them by the lawsuit." While the dispute is now over, the experience shed a harsh light on labor conditions in China. At the same time, the response of the Chinese media, and China Business News in particular, points toward the emergence of some journalist freedoms in a nation that has historically seen news organizations as a mouthpiece for the state.[1]

Introduction

As Apple discovered, ethical issues can arise when companies do business in different nations. These issues are often a function of differences in economic development, politics, legal systems, and culture. While managers at Hongfujin were not breaking local laws, their treatment of employees was arguably unethical when judged by Western standards. Moreover, many would argue that it is unethical for a company like Apple to work with a foreign supplier that treats its employees poorly. Managers at Apple had already anticipated this kind of problem and had a code on labor standards in place. When news of the labor conditions at Hongfujin surfaced, Apple management responded appropriately, quickly auditing Hongfujin's operations and requiring that the company change certain practices—although a skeptic might wonder, however, why it took damaging news to get Apple to audit Hongfujin. Apple management should probably have been auditing Hongfujin's operations on a regular basis, which apparently they were not.

As we shall see repeatedly in this chapter, not all companies have been able to deal with ethical problems in as timely a manner as Apple. There are many examples of managers who made poor ethical decisions while engaged in international business. The term *ethics* refers to accepted principles of right or wrong that govern the conduct of a person, the members of a profession, or the actions of an organization. **Business ethics** are the accepted principles of right or wrong governing the conduct of businesspeople, and an **ethical strategy** is a strategy, or course of action, that does not violate these accepted principles. This chapter looks at how ethical issues should be incorporated into decision making in an international business. We start by looking at the source and nature of ethical issues in an international business. Next, we review the reasons for poor ethical decision making. Then we discuss different philosophical approaches to business ethics. We close the chapter by reviewing the different processes managers can adopt to make sure ethical considerations are incorporated into decision making in an international business firm.

Ethical Issues in International Business

Many of the ethical issues in international business are rooted in the fact that political systems, law, economic development, and culture vary significantly from nation to nation. What is considered normal practice in one nation may be considered unethical in another. Because they work for an institution that transcends national borders and cultures, managers in a multinational firm need to be particularly sensitive to these differences. In the international business setting, the most common ethical issues involve employment practices, human rights, environmental regulations, corruption, and the moral obligation of multinational corporations.

EMPLOYMENT PRACTICES

When work conditions in a host nation are clearly inferior to those in a multinational's home nation, what standards should be applied—those of the home nation, those of the host nation, or something in between? While few would suggest that pay and work conditions should be the same across nations, how much divergence is acceptable? For example, while 12-hour workdays, extremely low pay, and a failure to protect workers against toxic chemicals may be common in some developing nations, does this mean it is OK for a multinational to tolerate such working conditions in its subsidiaries there, or to condone it by using local subcontractors?

Like Apple, in the 1990s, Nike found itself the center of a storm of protests when news reports revealed that working conditions at many of its subcontractors were very poor. Typical of the allegations were those detailed in a *48 Hours* program that aired in 1996. The report painted a picture of young women at a Vietnamese subcontractor who worked with toxic materials six days a week in poor conditions for only 20 cents an hour. The report also stated that a living wage in Vietnam was at least $3 a day, an income that could not be achieved at the subcontractor without working substantial overtime. Nike and its subcontractors were not breaking any laws, but this report, and others like it, raised questions about the ethics of using sweatshop labor to make what were essentially fashion accessories. It may have been legal, but was it ethical to use subcontractors who by Western standards clearly exploited their workforce? Nike's critics thought not, and the company found itself the focus of a wave of demonstrations and consumer boycotts. These exposés surrounding Nike's use of subcontractors forced the company to reexamine its policies. Realizing that, even though it was breaking no law, its subcontracting policies were perceived as unethical, Nike's management established a code of conduct for Nike subcontractors and instituted annual monitoring by independent auditors of all subcontractors.[2]

As the Nike and Apple cases demonstrate, a strong argument can be made that it is not OK for a multinational firm to tolerate poor working conditions in its foreign operations, or those of subcontractors. However, this still leaves unanswered the question of what standards should be applied. We shall return to and consider this issue in more detail later in the chapter. For now, note that establishing minimal acceptable standards that safeguard the basic rights and dignity of employees, auditing foreign subsidiaries and subcontractors on a regular basis to make sure those standards are met, and taking corrective action if they are not is a good way to guard against ethical abuses. Another apparel company, Levi Strauss, has long taken such an approach. The company terminated a long-term contract with one of its large suppliers, the Tan family, after discovering that the Tans were allegedly forcing 1,200 Chinese and Filipino women to work 74 hours per week in guarded compounds on the Mariana Islands.[3]

HUMAN RIGHTS

Questions of human rights can arise in international business. Basic human rights still are not respected in many nations. Rights that we take for granted in developed nations, such as freedom of association, freedom of speech, freedom of assembly, freedom of movement, freedom from political repression, and so on, are by no means universally accepted (see Chapter 2 for details). One of the most obvious historic examples was South Africa during the days of white rule and apartheid, which did not end until 1994. The apartheid system denied basic political rights to the majority nonwhite population of South Africa, mandated segregation between whites and nonwhites, reserved certain occupations exclusively for whites, and prohibited blacks from being placed in positions where they would manage whites. Despite the odious nature of this system, Western businesses operated in South Africa. By the 1980s, however, many questioned the ethics of doing so. They argued that inward investment by foreign multinationals, by boosting the South African economy, supported the repressive apartheid regime.

Several Western businesses started to change their policies in the late 1970s and early 1980s.[4] General Motors, which had significant activities in South Africa, was at the forefront of this trend. GM adopted what came to be called the *Sullivan principles*, named after Leon Sullivan, a black Baptist minister and a member of GM's board of directors. Sullivan argued that it was ethically justified for GM to operate in South Africa so long as two conditions were fulfilled. First, the company should not obey the apartheid laws in its own South African operations (a form of passive resistance). Second, the company should do everything within its power to promote the abolition of apartheid laws. Sullivan's principles were widely adopted by U.S. firms operating in South Africa. The South African government, which clearly did not want to antagonize important foreign investors, ignored their violation of the apartheid laws.

However, after 10 years, Leon Sullivan concluded that simply following the principles was not sufficient to break down the apartheid regime and that any American company, even those adhering to his principles, could not ethically justify their continued presence in South Africa. Over the next few years, numerous companies divested their South African operations, including Exxon, General Motors, Kodak, IBM, and Xerox. At the same time, many state pension funds signaled they would no longer hold stock in companies that did business in South Africa, which helped persuade several companies to divest their South African operations. These divestments, coupled with the imposition of economic sanctions from the U.S. and other governments, contributed to the abandonment of white minority rule and apartheid in South Africa and the introduction of democratic elections in 1994. Thus, some argued that adopting an ethical stance helped improve human rights in South Africa.[5]

Although change has come in South Africa, many repressive regimes still exist in the world. Is it ethical for multinationals to do business in them? It is often argued that inward investment by a multinational can be a force for economic, political, and social progress that ultimately improves the rights of people in repressive regimes. This position was first discussed in Chapter 2, when we noted that economic progress in a nation could create pressure for democratization. In general, this belief suggests it is ethical for a multinational to do business in nations that lack the democratic structures and human rights records of developed nations. Investment in China, for example, is frequently justified on the grounds that although human rights groups often question China's human rights record, and although the country is not a democracy, continuing inward investment will help boost economic growth and raise living standards. These developments will ultimately create pressures from the Chinese people for more participative government, political pluralism, and freedom of expression and speech.

However, there is a limit to this argument. As in the case of South Africa, some regimes are so repressive that investment cannot be justified on ethical grounds. A current example would be Myanmar (formally known as Burma). Ruled by a military dictatorship for more than 45 years, Myanmar has one of the worst human rights records in the world. Beginning in the mid-1990s, many Western companies exited Myanmar, judging the human rights violations to be so extreme that doing business there cannot be justified on ethical grounds. (In contrast, the accompanying Management Focus looks at the controversy surrounding one company, Unocal, that chose to stay in Myanmar.) However, a cynic might note that Myanmar has a small economy and that divestment carries no great economic penalty for Western firms, unlike, for example, divestment from China.

Nigeria is another country where serious questions have arisen over the extent to which foreign multinationals doing business in the country have contributed to human rights violations. Most notably, the largest foreign oil producer in the country, Royal Dutch Shell, has been repeatedly criticized.[6] In the early 1990s, several ethnic groups in Nigeria, which was ruled by a military dictatorship, protested against foreign oil companies for causing widespread pollution and failing to invest in the communities from which they extracted oil. Shell reportedly requested the assistance of Nigeria's Mobile Police Force (MPF) to quell the demonstrations. According to the human rights group Amnesty International, the results were bloody. In 1990, the MPF put down protests against Shell in the village of Umuechem, killing 80 people and destroying 495 homes. In 1993, following protests in the Ogoni region of Nigeria that were designed to stop contractors from laying a new pipeline for Shell, the MPF raided the area to quell the unrest. In the chaos that followed, it has been alleged that 27 villages were razed, 80,000 Ogoni people displaced, and 2,000 people killed.

Nigerian women and children protest Royal Dutch/Shell in April 2004.

Critics argued that Shell shouldered some of the blame for the massacres. Shell never acknowledged this, and the MPF probably used the demonstrations as a pretext

MANAGEMENT FOCUS

Unocal in Myanmar

In 1995, Unocal, an oil and gas enterprise based in California, took a 29 percent stake in a partnership with the French oil company Total and state-owned companies from both Myanmar and Thailand to build a gas pipeline from Myanmar to Thailand. At the time, the $1 billion project was expected to bring Myanmar about $200 million in annual export earnings, a quarter of the country's total export earnings. The gas used domestically would increase Myanmar's generating capacity by 30 percent. Unocal made this investment when a number of other American companies were exiting Myanmar. Myanmar's government, a military dictatorship, had a reputation for brutally suppressing internal dissent. Citing the political climate, the apparel companies Levi Strauss and Eddie Bauer had both withdrawn from the country. However, as far as Unocal's management was concerned, the giant infrastructure project would generate healthy returns for the company and, by boosting economic growth, a better life for Myanmar's 43 million people. Moreover, while Levi Strauss and Eddie Bauer could easily shift production of clothes to another low-cost location, Unocal argued it had to go where the oil and gas were located.

However, Unocal's investment quickly became highly controversial. Under the terms of the contract, the government of Myanmar was contractually obliged to clear a corridor for the pipeline through Myanmar's tropical forests and to protect the pipeline from attacks by the government's enemies. According to human rights groups, the Myanmar army forcibly moved villages and ordered hundreds of local peasants to work on the pipeline in conditions that were no better than slave labor. Those who refused suffered retaliation. News reports cite the case of one woman who was thrown into a fire, along with her baby, after her husband tried to escape from troops forcing him to work on the project. The baby died and she suffered burns. Other villagers report being beaten, tortured, raped, and otherwise mistreated under the alleged slave labor conditions.

In 1996, human rights activists brought a lawsuit against Unocal in the United States on behalf of 15 Myanmar villagers who had fled to refugee camps in Thailand. The suit claimed that Unocal was aware of what was going on, even if it did not participate or condone it, and that awareness was enough to make Unocal in part responsible for the alleged crimes. The presiding judge dismissed the case, arguing that Unocal could not be held liable for the actions of a foreign government against its own people—although the judge did note that Unocal was indeed aware of what was going on in Myanmar. The plaintiffs appealed, and in late 2003 the case wound up at a superior court. In 2005 the case was settled out of court for an undisclosed amount.[11]

for punishing an ethnic group that had been agitating against the central government for some time. Nevertheless, these events did prompt Shell to look at its own ethics and to set up internal mechanisms to ensure that its subsidiaries acted in a manner that was consistent with basic human rights.[7] More generally, the question remains, what is the responsibility of a foreign multinational when operating in a country where basic human rights are trampled on? Should the company be there at all, and if it is there, what actions should it take to avoid the situation Shell found itself in?

ENVIRONMENTAL POLLUTION

Ethical issues arise when environmental regulations in host nations are inferior to those in the home nation. Many developed nations have substantial regulations governing the emission of pollutants, the dumping of toxic chemicals, the use of toxic materials in the workplace, and so on. Those regulations are often lacking in developing nations, and according to critics, the result can be higher levels of pollution from the operations of multinationals than would be allowed at home. For example, consider again the case of foreign oil companies in Nigeria. According to a 1992 report prepared by environmental activists in the Niger Delta region of Nigeria,

> Apart from air pollution from the oil industry's emissions and flares day and night, producing poisonous gases that are silently and systematically wiping out vulnerable airborne biota and endangering the life of plants, game, and man himself, we have widespread water pollution and soil/land pollution that results in the death of most aquatic eggs and juvenile stages of the life of fin fish and shell fish on the one hand, whilst, on the other hand, agricultural land contaminated with oil spills becomes dangerous for farming, even where they continue to produce significant yields.[8]

The implication inherent in this description is that the pollution controls foreign companies applied in Nigeria were much more lax than those applied in developed nations.

Should a multinational feel free to pollute in a developing nation? (To do so hardly seems ethical.) Is there a danger that amoral management might move production to a developing nation precisely because costly pollution controls are not required, and the company is therefore free to despoil the environment and perhaps endanger local people in its quest to lower production costs and gain a competitive advantage? What is the right and moral thing to do in such circumstances—pollute to gain an economic advantage, or make sure that foreign subsidiaries adhere to common standards regarding pollution controls?

These questions take on added importance because some parts of the environment are a public good that no one owns, but anyone can despoil. No one owns the atmosphere or the oceans, but polluting both, no matter where the pollution originates, harms all.[9] The atmosphere and oceans can be viewed as a global commons from which everyone benefits but for which no one is specifically responsible. In such cases, a phenomenon known as the *tragedy of the commons* becomes applicable. The tragedy of the commons occurs when individuals overuse a resource held in common by all, but owned by no one, resulting in its degradation. The phenomenon was first named by Garrett Hardin when describing a particular problem in 16th-century England. Large open areas, called commons, were free for all to use as pasture. The poor put out livestock on these commons and supplemented their meager incomes. It was advantageous for each to put out more and more livestock, but the social consequence was far more livestock than the commons could handle. The result was overgrazing, degradation of the commons, and the loss of this much-needed supplement.[10]

In the modern world, corporations can contribute to the global tragedy of the commons by moving production to locations where they are free to pump pollutants into the atmosphere or dump them in oceans or rivers, thereby harming these valuable global commons. While such action may be legal, is it ethical? Again, such actions seem to violate basic societal notions of ethics and social responsibility.

CORRUPTION

As noted in Chapter 2, corruption has been a problem in almost every society in history, and it continues to be one today.[12] There always have been and always will be corrupt government officials. International businesses can and have gained economic advantages by making payments to those officials. A classic example concerns a well-publicized incident in the 1970s. Carl Kotchian, the president of Lockheed, made a $12.5 million payment to Japanese agents and government officials to secure a large order for Lockheed's TriStar jet from Nippon Air. When the payments were discovered, U.S. officials charged Lockheed with falsification of its records and tax violations. Although such payments were supposed to be an accepted business practice in Japan (they might be viewed as an exceptionally lavish form of gift giving), the revelations created a scandal there too. The government ministers in question were criminally charged, one committed suicide, the government fell in disgrace, and the Japanese people were outraged. Apparently, such a payment was not an accepted way of doing business in Japan! The payment was nothing more than a bribe, paid to corrupt officials, to secure a large order that might otherwise have gone to another manufacturer, such as Boeing. Kotchian clearly engaged in unethical behavior, and to argue that the payment was an "acceptable form of doing business in Japan" was self-serving and incorrect.

The Lockheed case was the impetus for the 1977 passage of the **Foreign Corrupt Practices Act** in the United States, which we first discussed in Chapter 2. The act outlawed the paying of bribes to foreign government officials to gain business. Some U.S. businesses immediately objected that the act would put U.S. firms at a competitive disadvantage (there is no evidence that this actually occurred).[13] The act was subsequently amended to allow for "facilitating payments." Sometimes known as speed money or grease payments, facilitating payments are *not* payments to secure contracts that would not otherwise be secured, nor are they payments to obtain exclusive preferential treatment. Rather they are payments to ensure receiving the standard treatment that a business ought to receive from a foreign government, but might not receive due to the obstruction of a foreign official.

In 1997, the trade and finance ministers from the member states of the Organization for Economic Cooperation and Development (OECD) followed the U.S. lead and adopted the **Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.**[14] The convention, which went into force in 1999, obliges member states and other signatories to make the bribery of foreign public officials a criminal offense. The convention excludes facilitating payments made to expedite routine government action from the convention. To date, some 36 countries have signed the convention, six of whom are not OECD members.

While facilitating payments, or speed money, are excluded from both the Foreign Corrupt Practices Act and the OECD convention on bribery, the ethical implications of making such payments are unclear. In many countries, payoffs to government officials in the form of speed money are a part of life. One can argue that not investing because government officials demand speed money ignores the fact that such investment can bring substantial benefits to the local populace in terms of income and jobs. From a pragmatic standpoint, giving bribes, although a little evil, might be the price that must be paid to do a greater good (assuming the investment creates jobs where none existed and assuming the practice is not illegal). Several economists advocate this reasoning, suggesting that in the context of pervasive and cumbersome regulations in developing countries, corruption may improve efficiency and help growth! These economists theorize that in a country where preexisting political structures distort or limit the workings of the market mechanism, corruption in the form of black-marketeering, smuggling, and side payments to government bureaucrats to "speed up" approval for business investments may enhance welfare.[15] Arguments such as this persuaded the U.S. Congress to exempt facilitating payments from the Foreign Corrupt Practices Act.

In contrast, other economists have argued that corruption reduces the returns on business investment and leads to low economic growth.[16] In a country where corruption is common, unproductive bureaucrats who demand side payments for granting the enterprise permission to operate may siphon off the profits from a business activity. This reduces businesses' incentive to invest and may retard a country's economic growth rate. One study of the connection between corruption and economic growth in 70 countries found that corruption had a significant negative impact on a country's growth rate.[17]

Given the debate and the complexity of this issue, one again might conclude that generalization is difficult and the demand for speed money creates a genuine ethical dilemma. Yes, corruption is bad, and yes, it may harm a country's economic development, but yes, there are also cases where side payments to government officials can remove the bureaucratic barriers to investments that create jobs. However, this pragmatic stance ignores the fact that corruption tends to corrupt both the bribe giver and the bribe taker. Corruption feeds on itself, and once an individual starts down the road of corruption, pulling back may be difficult if not impossible. This argument strengthens the ethical case for never engaging in corruption, no matter how compelling the benefits might seem.

Many multinationals have accepted this argument. The large oil multinational, BP, for example, has a zero-tolerance approach toward facilitating payments. Other corporations have a more nuanced approach. For example, consider the following from the code of ethics at Dow Corning:

> Dow Corning employees will not authorize or give payments or gifts to government employees or their beneficiaries or anyone else in order to obtain or retain business. Facilitating payments to expedite the performance of routine services are strongly discouraged. In countries where local business practice dictates such payments and there is no alternative, facilitating payments are to be for the minimum amount necessary and must be accurately documented and recorded.[18]

This statement allows for facilitating payments when "there is no alternative," although they are strongly discouraged.

MORAL OBLIGATIONS

Multinational corporations have power that comes from their control over resources and their ability to move production from country to country. Although that power is constrained not only by laws and regulations but also by the discipline of the market and the competitive process, it is nevertheless substantial. Some moral philosophers argue that with power comes the social responsibility for multinationals to give something back to the societies that enable them to prosper and grow. The concept of **social responsibility** refers to the idea that businesspeople should consider the social consequences of economic actions when making business decisions, and that there should be a presumption in favor of decisions that have both good economic and social consequences.[19] In its purest form, social responsibility can be supported for its own sake simply because it is the right way for a business to behave. Advocates of this approach argue that businesses, particularly large successful businesses, need to recognize their *noblesse oblige* and give something back to the societies that have made their success possible. *Noblesse oblige* is a French term that refers to honorable and benevolent behavior considered the responsibility of people of high (noble) birth. In a business setting, it is taken to mean benevolent behavior that is the responsibility of *successful* enterprises. Businesspeople have long recognized the concept, resulting in a substantial and venerable history of corporate giving to society and social investments designed to enhance the welfare of the communities in which businesses operate.

However, some multinationals have abused their power for private gain. The most famous historic example relates to one of the earliest multinationals, the British East India Company. Established in 1600, the East India Company grew to dominate the entire Indian subcontinent in the 19th century. At the height of its power, the company deployed over 40 warships, possessed the largest standing army in the world, was the de facto ruler of India's 240 million people, and even hired its own church bishops, extending its dominance into the spiritual realm.[20]

Power itself is morally neutral—how power is used is what matters. It can be used in a positive way to increase social welfare, which is ethical, or it can be used in a manner that is ethically and morally suspect. Consider the case of News Corporation, one of the largest media conglomerates in the world, which is profiled in the accompanying Management Focus. The power of media companies derives from their ability to shape public perceptions by the material they choose to publish. News Corporation founder and CEO Rupert Murdoch has long considered China to be one of the most promising media markets in the world and has sought permission to expand News Corporation's operations in China, particularly the satellite broadcasting operations of Star TV. Some critics believe that Murdoch used the power of News Corporation in an unethical way to attain this objective.

Some multinationals have acknowledged a moral obligation to use their power to enhance social welfare in the communities where they do business. BP, one of the world's largest oil companies, has made it part of the company policy to undertake "social investments" in the countries where it does business.[21] In Algeria, BP has been investing in a major project to develop gas fields near the desert town of Salah. When the company noticed the lack of clean water in Salah, it built two desalination plants to provide drinking water for the

MANAGEMENT FOCUS

News Corporation in China

Rupert Murdoch built News Corporation into one of the largest media conglomerates in the world with interests that include newspapers, publishing, and television broadcasting. According to critics, however, Murdoch abused his power to gain preferential access to the Chinese media market by systematically suppressing media content that was critical of China and publishing material designed to ingratiate the company with the Chinese leadership.

In 1994, News Corporation excluded BBC news broadcasts from Star TV coverage in the region after it had become clear that Chinese politicians were unhappy with the BBC's continual reference to repression in China and, most notably, the 1989 massacre of student protesters for democracy in Beijing's Tiananmen Square. In 1995, News Corporation's book publishing subsidiary, HarperCollins, published a flattering biography of Deng Xiaoping, the former leader of China, written by his daughter. Then in 1998, HarperCollins dropped plans to publish the memoirs of Chris Patten, the last governor of Hong Kong before its transfer to the Chinese. Patten, a critic of Chinese leaders, had aroused their wrath by attempting to introduce a degree of democracy into the administration of the old British territory before its transfer back to China in 1997.

In a 1998 interview in *Vanity Fair,* Murdoch took another opportunity to ingratiate himself with the Chinese leadership when he described the Dalai Lama, the exiled leader of Chinese-occupied Tibet, as "a very political old monk shuffling around in Gucci shoes." On the heels of this, in 2001 Murdoch's son James, who was in charge of running Star TV, made disparaging remarks about Falun Gong, a spiritual movement involving breathing exercises and meditation that had become so popular in China that the Communist regime regarded it as a political threat and suppressed its activities. According to James Murdoch, Falun Gong was a "dangerous," "apocalyptic cult" that "clearly does not have the success of China at heart."

Critics argued that these events were all part of a deliberate effort on the part of News Corporation to curry favor with the Chinese. The company received its reward in 2001 when Star TV struck an agreement with the Chinese government to launch a Mandarin-language entertainment channel for the affluent southern coastal province of Guangdong. Earlier that year, China's leader, Jiang Zemin, had publicly praised Murdoch and Star TV for their efforts "to present China objectively and to cooperate with the Chinese press."

Once in China, News Corp was soon tugging at the constraints imposed on it by the Chinese government. Starting in 2002, News Corp set up shell companies, owned by News Corp employees, which then resold News Corp programming to local cable TV networks throughout China, in direct violation of Chinese regulations. Payments, sometimes in the form of briefcases stuffed with cash, were channeled to News Corp through the shell companies. One such deal involved selling News Corp programming through a shell company known as Runde Investment Corporation to a nationwide satellite TV channel, Qinghai Satellite, based in the remote Qinghai province of China. Runde was partly owned by the son of the former hard-line Communist Party propaganda minister, Ding Guangen. If News Corp was hoping that its political connections would help it to get away with these actions, it was badly disappointed. In 2005, Chinese authorities raided News Corp's headquarters and seized documents and equipment. They also quickly terminated the deal with Qinghai Satellite.[22]

local community and distributed containers to residents so they could take water from the plants to their homes. There was no economic reason for BP to make this social investment, but the company believes it is morally obligated to use its power in constructive ways. The action, while a small thing for BP, is a very important thing for the local community.

Ethical Dilemmas

The ethical obligations of a multinational corporation toward employment conditions, human rights, corruption, environmental pollution, and the use of power are not always clear-cut. There may be no agreement about accepted ethical principles. From an international business perspective, some argue that what is ethical depends upon one's cultural perspective.[23] In the United States, it is considered acceptable to execute murderers but in many cultures this is not acceptable—execution is viewed as an affront to human dignity and the death penalty is outlawed. Many Americans find this attitude very strange, but many Europeans find the American approach barbaric. For a more business-oriented example, consider the practice of "gift giving" between the parties to a business negotiation. While this is considered right and proper behavior in many Asian cultures, some Westerners view the practice as a form of bribery, and therefore unethical, particularly if the gifts are substantial.

Managers often confront very real ethical dilemmas where the appropriate course of action is not clear. For example, imagine that a visiting American executive finds that a foreign subsidiary in a poor nation has hired a 12-year-old girl to work on a factory floor. Appalled to find that the subsidiary is using child labor in direct violation of the company's own ethical code, the American instructs the local manager to replace the child with an adult. The local manager dutifully complies. The girl, an orphan, who is the only breadwinner for herself and her 6-year-old brother, is unable to find another job, so in desperation she turns to prostitution. Two years later she dies of AIDS. Meanwhile, her brother takes up begging. He encounters the American while begging outside the local McDonald's. Unaware that this was the man responsible for his fate, the boy begs him for money. The American quickens his pace and walks rapidly past the outstretched hand into the McDonald's, where he orders a quarter-pound cheeseburger with fries and a cold milk shake. A year later, the boy contracts tuberculosis and dies.

Had the visiting American understood the gravity of the girl's situation, would he still have requested her replacement? Perhaps not! Would it have been better, therefore, to stick with the status quo and allow the girl to continue working? Probably not, because that would have violated the reasonable prohibition against child labor found in the company's own ethical code. What, then, would have been the right thing to do? What was the obligation of the executive given this ethical dilemma?

There is no easy answer to these questions. That is the nature of **ethical dilemmas**—they are situations in which none of the available alternatives seems ethically acceptable.[24] In this case, employing child labor was not acceptable, but neither was denying the child her only source of income. What the American executive needed, what all managers need, was a moral compass, or perhaps an ethical algorithm, that would guide him through such an ethical dilemma to find an acceptable solution. Later we will outline what such a moral compass, or ethical algorithm, might look like. For now, it is enough to note that ethical dilemmas exist because many real-world decisions are complex, difficult to frame, and involve first-, second-, and third-order consequences that are hard to quantify. Doing the right thing, or even knowing what the right thing might be, is often far from easy.[25]

The Roots of Unethical Behavior

As we have seen, examples abound of managers behaving in a manner that might be judged unethical in an international business setting. Why do managers behave in an unethical manner? There is no simple answer to this question, for the causes are complex, but some generalizations can be made (see Figure 4.1).[26]

PERSONAL ETHICS

Business ethics are not divorced from *personal ethics*, which are the generally accepted principles of right and wrong governing the conduct of individuals. As individuals, we are typically taught that it is wrong to lie and cheat—it is unethical—and that it is right to behave with integrity and honor and to stand up for what we believe to be right. This is generally true across societies. The personal ethical code that guides our behavior comes from a number of sources, including our parents, our schools, our religion, and the media. Our personal ethical code exerts a profound influence on the way we behave as businesspeople. An individual with a strong sense of personal ethics is less likely to behave in an

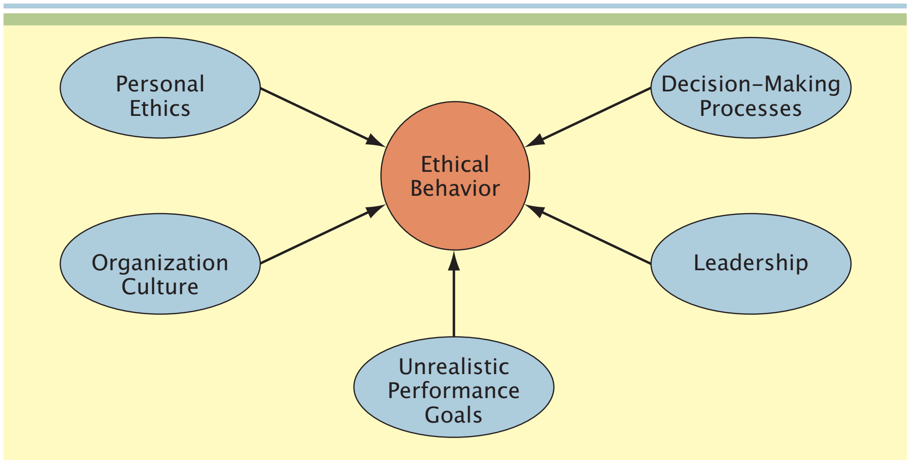


FIGURE 4.1

Determinants of Ethical Behavior

unethical manner in a business setting. It follows that the first step to establishing a strong sense of business ethics is for a society to emphasize strong personal ethics.

Home-country managers working abroad in multinational firms (expatriate managers) may experience more than the usual degree of pressure to violate their personal ethics. They are away from their ordinary social context and supporting culture, and they are psychologically and geographically distant from the parent company. They may be based in a culture that does not place the same value on ethical norms important in the manager's home country, and they may be surrounded by local employees who have less rigorous ethical standards. The parent company may pressure expatriate managers to meet unrealistic goals that can only be fulfilled by cutting corners or acting unethically. For example, to meet centrally mandated performance goals, expatriate managers might give bribes to win contracts or establish working conditions and environmental controls that are below minimal acceptable standards. Local managers might encourage the expatriate to adopt such behavior. Due to its geographical distance, the parent company may be unable to see how expatriate managers are meeting goals, or they may choose not to see how they are doing so, allowing such behavior to flourish and persist.

DECISION-MAKING PROCESSES

Several studies of unethical behavior in a business setting have concluded that businesspeople sometimes do not realize they are behaving unethically, primarily because they simply fail to ask, "Is this decision or action ethical?"[27] Instead, they apply a straightforward business calculus to what they perceive to be a business decision, forgetting that the decision may also have an important ethical dimension. The fault lies in processes that do not incorporate ethical considerations into business decision making. This may have been the case at Nike when managers originally made subcontracting decisions (see the earlier discussion). Those decisions were probably made based on good economic logic. Subcontractors were probably chosen based on business variables such as cost, delivery, and product quality, and the key managers simply failed to ask, "How does this subcontractor treat its workforce?" If they thought about the question at all, they probably reasoned that it was the subcontractor's concern, not theirs. (For another example of a business decision that may have been unethical, see the Management Focus describing Pfizer's decision to test an experimental drug on children suffering from meningitis in Nigeria.)

ORGANIZATION CULTURE

The climate in some businesses does not encourage people to think through the ethical consequences of business decisions. This brings us to the third cause of unethical behavior in businesses—an organizational culture that deemphasizes business ethics, reducing

MANAGEMENT FOCUS

Pfizer's Drug Testing Strategy in Nigeria

The drug development process is long, risky, and expensive. It can take 10 years and cost in excess of $500 million to develop a new drug. Moreover, between 80 and 90 percent of drug candidates fail in clinical trials. Pharmaceutical companies rely upon a handful of successes to pay for their failures. Among the most successful of the world's pharmaceutical companies is New York–based Pfizer. Given the risks and costs of developing a new drug, pharmaceutical companies will jump at opportunities to reduce them, and in 1996 Pfizer thought it saw one.

Pfizer had been developing a novel antibiotic, Trovan, that was proving to be useful in treating a wide range of bacterial infections. Wall Street analysts were predicting that Trovan could be a blockbuster, one of a handful of drugs capable of generating sales of more than $1 billion a year. In 1996, Pfizer was pushing to submit data on Trovan's efficacy to the Food and Drug Administration (FDA) for review. A favorable review would allow Pfizer to sell the drug in the United States, the world's largest market. Pfizer wanted the drug to be approved for both adults and children, but it was having trouble finding sufficient numbers of sick children in the United States to test the drug on. Then in early 1996, a researcher at Pfizer read about an emerging epidemic of bacterial meningitis in Kano, Nigeria. This seemed like a quick way to test the drug on a large number of sick children.

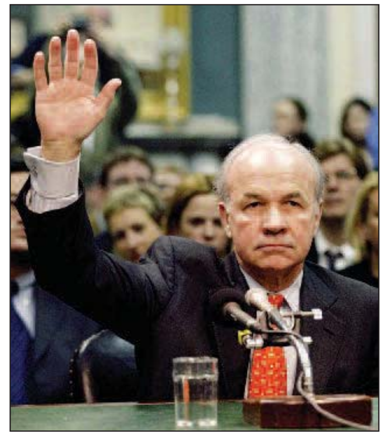
Within weeks a team of six doctors had flown to Kano and were administering the drug, in oral form, to children with meningitis. Desperate for help, Nigerian authorities allowed Pfizer to give the drug to children (the epidemic would ultimately kill nearly 16,000 people). Over the next few weeks, Pfizer treated 198 children. The protocol called for half the patients to get Trovan and half to get a comparison antibiotic already approved for the treatment of children. After a few weeks, the Pfizer team left, the experiment complete. Trovan seemed to be about as effective and safe as the already approved antibiotic. The data from the trial were put into a package with data from other trials of Trovan and delivered to the FDA.

Questions were soon raised about the nature of Pfizer's experiment. Allegations charged that the Pfizer team kept children on Trovan, even after they failed to show a response to the drug, instead of switching them quickly to another drug. The result, according to critics, was that some children died who might have been saved had they been taken off Trovan sooner. Questions were also raised about the safety of the oral formulation of Trovan, which some doctors feared might lead to arthritis in children. Fifteen children who took Trovan showed signs of joint pain during the experiment, three times the rate of children taking the other antibiotic. Then there were questions about consent. The FDA requires that patient (or parent) consent be given before patients are enrolled in clinical trials, no matter where in the world the trials are conducted. Critics argue that in the rush to get the trial established in Nigeria, Pfizer did not follow proper procedures, and that many parents of the infected children did not know their children were participating in a trial for an experimental drug. Many of the parents were illiterate, could not read the consent forms, and had to rely upon the questionable translation of the Nigerian nursing staff. Pfizer rejected these charges and contends that it did nothing wrong.

Trovan was approved by the FDA for use in adults in 1997, but it was never approved for use in children. Launched in 1998, by 1999 there were reports that up to 140 patients in Europe had suffered liver damage after taking Trovan. The FDA subsequently restricted the use of Trovan to those cases where the benefits of treatment outweighed the risk of liver damage. European regulators banned sales of the drug.[29]

all decisions to the purely economic. The term **organization culture** refers to the values and norms that employees of an organization share. You will recall from Chapter 3 that *values* are abstract ideas about what a group believes to be good, right, and desirable, while *norms* are the social rules and guidelines that prescribe appropriate behavior in particular situations. Just as societies have cultures, so do business organizations. Together, values and norms shape the culture of a business organization, and that culture has an important influence on the ethics of business decision making.

Author Robert Bryce has explained how the organization culture at now-bankrupt multinational energy company Enron was built on values that emphasized greed and deception.[28] According to Bryce, the tone was set by top managers who engaged in self-dealing to enrich themselves and their own families. Bryce tells how former Enron CEO Kenneth Lay made sure his own family benefited handsomely from Enron. Much of Enron's corporate travel business was handled by a travel agency in which Lay's sister was a part-owner. When an internal auditor recommended that the company could do better by using another travel agency, he soon found himself out of a job. In 1997, Enron acquired a company owned by Kenneth Lay's son, Mark Lay, which was trying to establish a business trading paper and pulp products. At the time, Mark Lay and another company he controlled were targets of a federal criminal investigation of bankruptcy fraud and embezzlement. As part of the deal, Enron hired Mark Lay as an executive with a three-year contract that guaranteed him at least $1 million in pay over that period, plus options to purchase about 20,000 shares of Enron. Bryce also details how Lay's grown daughter used an Enron jet to transport her king-sized bed to France. With Kenneth Lay as an example, it is perhaps not surprising that self-dealing soon became endemic at Enron. The most notable example was Chief Financial Officer Andrew Fastow, who set up "off balance sheet" partnerships that not only hid Enron's true financial condition from investors but also paid tens of millions of dollars directly to Fastow. (Fastow was subsequently indicted by the government for criminal fraud and went to jail.)



Former Enron CEO Kenneth Lay was charged with a variety of criminal deeds.

UNREALISTIC PERFORMANCE EXPECTATIONS

A fourth cause of unethical behavior has already been hinted at—it is pressure from the parent company to meet unrealistic performance goals that can be attained only by cutting corners or acting in an unethical manner. Again, Bryce discusses how this may have occurred at Enron. Lay's successor as CEO, Jeff Skilling, put a performance evaluation system in place that weeded out 15 percent of underperformers every six months. This created a pressure-cooker culture with a myopic focus on short-run performance, and some executives and energy traders responded to that pressure by falsifying their performance—inflating the value of trades, for example—to make it look as if they were performing better than was actually the case.

The lesson from the Enron debacle is that an organizational culture can legitimize behavior that society would judge as unethical, particularly when the culture is combined with a focus on unrealistic performance goals, such as maximizing short-term economic performance, no matter what the costs. In such circumstances, there is a greater than average probability that managers will violate their own personal ethics and engage in unethical behavior. Conversely, an organization culture can do just the opposite and reinforce the need for ethical behavior. At Hewlett-Packard, for example, Bill Hewlett and David Packard, the company's founders, propagated a set of values known as The HP Way. These values, which shape the way business is conducted both within and by the corporation, have an important ethical component. Among other things, they stress the need for confidence in and respect for people, open communication, and concern for the individual employee.

LEADERSHIP

The Enron and Hewlett-Packard examples suggest a fifth root cause of unethical behavior—leadership. Leaders help to establish the culture of an organization, and they set the example that others follow. Other employees in a business often take their cue from business leaders, and if those leaders do not behave in an ethical manner, they might not either. It is not what leaders say that matters, but what they do. Enron, for example, had a code of ethics that Kenneth Lay himself often referred to, but Lay's own actions to enrich family members spoke louder than any words.

Philosophical Approaches to Ethics

We shall look at several different approaches to business ethics here, beginning with some that can best be described as straw men, which either deny the value of business ethics or apply the concept in a very unsatisfactory way. Having discussed, and dismissed, the straw men, we then move on to consider approaches that most moral philosophers favor and that form the basis for current models of ethical behavior in international businesses.

STRAW MEN

Business ethics scholars discuss some approaches to business ethics primarily to demonstrate that they offer inappropriate guidelines for ethical decision making in a multinational enterprise. Four such approaches to business ethics are commonly discussed in the literature: the Friedman doctrine, cultural relativism, the righteous moralist, and the naive immoralist. All of these approaches have some inherent value, but all are unsatisfactory in important ways. Nevertheless, sometimes companies adopt these approaches.

The Friedman Doctrine

The Nobel Prize–winning economist Milton Friedman wrote an article in 1970 that has since become a classic straw man that business ethics scholars outline only to tear down.[30] Friedman's basic position is that the only social responsibility of business is to increase profits, so long as the company stays within the rules of law. He explicitly rejects the idea that businesses should undertake social expenditures beyond those mandated by the law and required for the efficient running of a business. For example, his arguments suggest that improving working conditions beyond the level required by the law *and* necessary to maximize employee productivity will reduce profits and is therefore not appropriate. His belief is that a firm should maximize its profits because that is the way to maximize the returns that accrue to the owners of the firm, its stockholders. If stockholders then wish to use the proceeds to make social investments, that is their right, according to Friedman, but managers of the firm should not make that decision for them.

Although Friedman is talking about social responsibility, rather than business ethics per se, many business ethics scholars equate social responsibility with ethical behavior and thus believe Friedman is also arguing against business ethics. However, the assumption that Friedman is arguing against ethics is not quite true, for Friedman does state,

> There is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say that it engages in open and free competition without deception or fraud.[31]

In other words, Friedman states that businesses should behave in an ethical manner and not use deception and fraud.

Nevertheless, Friedman's arguments do break down under examination. This is particularly true in international business where the "rules of the game" are not well established and differ from country to county. Consider again the case of sweatshop labor. Child labor may not be against the law in a developing nation, and maximizing productivity may not require that a multinational firm stop using child labor in that country, but it is still immoral to use child labor because the practice conflicts with widely held views about what is the right and proper thing to do. Similarly, there may be no rules against pollution in a developed nation and spending money on pollution control may reduce the profit rate of the firm, but generalized notions of morality would hold that it is still unethical to dump toxic pollutants into rivers or foul the air with gas releases. In addition to the local consequences of such pollution, which may have serious health effects for the surrounding population, it also has global consequences as pollutants degrade those two global commons so important to us all—the atmosphere and the oceans.

Cultural Relativism

Another straw man that business ethics scholars often raise is **cultural relativism,** which is the belief that ethics are nothing more than the reflection of a culture—all ethics are culturally determined—and that accordingly, a firm should adopt the ethics of the culture in which it is operating.[32] This approach is often summarized by the maxim *when in Rome do as the Romans do.* As with Friedman's approach, cultural relativism does not stand up to a closer look. At its extreme, cultural relativism suggests that if a culture supports slavery, it is OK to use slave labor in a country. Clearly, it is not! Cultural relativism implicitly rejects the idea that universal notions of morality transcend different cultures, but, as we shall argue later in the chapter, some universal notions of morality are found across cultures.

While dismissing cultural relativism in its most sweeping form, some ethicists argue that there is residual value in this approach.[33] As we noted in Chapter 3, societal values and norms do vary from culture to culture—customs do differ, so it might follow that certain business practices are ethical in one country, but not another. Indeed, the facilitating payments allowed in the Foreign Corrupt Practices Act can be seen as an acknowledgment that in some countries, the payment of speed money to government officials is necessary to get business done, and if not ethically desirable, it is at least ethically acceptable.

However, not all ethicists or companies agree with this pragmatic view. As noted earlier, oil company BP explicitly states it will not make facilitating payments, no matter what the prevailing cultural norms are. In 2002, BP enacted a zero-tolerance policy for facilitation payments, primarily on the basis that such payments are a low-level form of corruption, and thus cannot be justified because corruption corrupts both the bribe giver and the bribe taker and perpetuates the corrupt system. As BP notes on its Web site, because of its zero-tolerance policy:

> Some oil product sales in Vietnam involved inappropriate commission payments to the managers of customers in return for placing orders with BP. These were stopped during 2002 with the result that BP failed to win certain tenders with potential profit totaling $300k. In addition, two sales managers resigned over the issue. The business, however, has recovered using more traditional sales methods and has exceeded its targets at year-end.[34]

BP's experience suggests that companies should not use cultural relativism as an argument for justifying behavior that is clearly based upon suspect ethical grounds, even if that behavior is both legal and routinely accepted in the country where the company is doing business.

The Righteous Moralist

A **righteous moralist** claims that a multinational's home-country standards of ethics are the appropriate ones for companies to follow in foreign countries. This approach is typically associated with managers from developed nations. While this seems reasonable at first blush, the approach can create problems. Consider the following example: An American bank manager was sent to Italy, where he was appalled to learn that the local branch's accounting department recommended grossly underreporting the bank's profits for income tax purposes.[35] The manager insisted that the bank report its earnings accurately, American style. When he was called by the Italian tax department to the firm's tax hearing, he was told the firm owed three times as much tax as it had paid, reflecting the department's standard assumption that each firm underreports its earnings by two-thirds. Despite his protests, the new assessment stood. In this case, the righteous moralist has run into a problem caused by the prevailing cultural norms in the country where he is doing business. How should he respond? The righteous moralist would argue for maintaining the position, while a more pragmatic view might be that in this case, the right thing to do is to follow the prevailing cultural norms, since there is a big penalty for not doing so.

The main criticism of the righteous moralist approach is that its proponents go too far. While there are some universal moral principles that should not be violated, it does not always follow that the appropriate thing to do is adopt home-country standards. For example, U.S. laws set down strict guidelines with regard to minimum wage and working conditions. Does this mean it is ethical to apply the same guidelines in a foreign country, paying people the same as they are paid in the United States, providing the same benefits and working conditions? Probably not, because doing so might nullify the reason for investing in that country and therefore deny locals the benefits of inward investment by the multinational. Clearly, a more nuanced approach is needed.

The Naive Immoralist

A **naive immoralist** asserts that if a manager of a multinational sees that firms from other nations are not following ethical norms in a host nation, that manager should not either. The classic example to illustrate the approach is known as the drug lord problem. In one variant of this problem, an American manager in Colombia routinely pays off the local drug lord to guarantee that his plant will not be bombed and that none of his employees will be kidnapped. The manager argues that such payments are ethically defensible because everyone is doing it.

The objection to the manager's behavior is twofold. First, to say that an action is ethically justified if everyone is doing it is not sufficient. If firms in a country routinely employ 12-year-olds and make them work 10-hour days, is it therefore ethically defensible to do the same? Obviously not, and the company does have a clear choice. It does not have to abide by local practices, and it can decide not to invest in a country where the practices are particularly odious. Second, the multinational must recognize that it does have the ability to change the prevailing practice in a country. It can use its power for a positive moral purpose. This is what BP is doing by adopting a zero-tolerance policy with regard to facilitating payments. BP is stating that the prevailing practice of making facilitating payments is ethically wrong, and it is incumbent upon the company to use its power to try to change the standard. While some might argue that such an approach smells of moral imperialism and a lack of cultural sensitivity, if it is consistent with widely accepted moral standards in the global community, it may be ethically justified.

To return to the drug lord problem, an argument can be made that it is ethically defensible to make such payments, not because everyone else is doing so but because not doing so would cause greater harm (i.e., the drug lord might seek retribution and engage in killings and kidnappings). Another solution to the problem is to refuse to invest in a country where the rule of law is so weak that drug lords can demand protection money. This solution, however, is also imperfect, for it might mean denying the law-abiding citizens of that country the benefits associated with inward investment by the multinational (i.e., jobs, income, greater economic growth and welfare). Clearly, the drug lord problem constitutes one of those intractable ethical dilemmas where there is no obvious right solution, and managers need a moral compass to help them find an acceptable solution to the dilemma.

UTILITARIAN AND KANTIAN ETHICS

In contrast to the straw men just discussed, most moral philosophers see value in utilitarian and Kantian approaches to business ethics. These approaches were developed in the 18th and 19th centuries and although they have been largely superseded by more modern approaches, they form part of the tradition upon which newer approaches have been constructed.

The utilitarian approach to business ethics dates to philosophers such as David Hume (1711–1776), Jeremy Bentham (1784–1832), and John Stuart Mill (1806–1873). **Utilitarian approaches** to ethics hold that the moral worth of actions or practices is determined by their consequences.[36] An action is judged desirable if it leads to the best possible balance of good consequences over bad consequences. Utilitarianism is committed to the maximization of good and the minimization of harm. Utilitarianism recognizes that actions have multiple consequences, some of which are good in a social sense and some of which are harmful. As a philosophy for business ethics, it focuses attention on the need to weigh carefully all the social benefits and costs of a business action and to pursue only those actions where the benefits outweigh the costs. The best decisions, from a utilitarian perspective, are those that produce the greatest good for the greatest number of people.

Many businesses have adopted specific tools such as cost–benefit analysis and risk assessment that are firmly rooted in a utilitarian philosophy. Managers often weigh the benefits and costs of an action before deciding whether to pursue it. An oil company considering drilling in an Alaskan wildlife preserve must weigh the economic benefits of increased oil production and the creation of jobs against the costs of environmental degradation in a fragile ecosystem. An agricultural biotechnology company such as Monsanto must decide whether the benefits of genetically modified crops that produce natural pesticides outweigh the risks. The benefits include increased crop yields and reduced need for chemical fertilizers. The risks include the possibility that Monsanto's insect-resistant crops might make matters worse over time if insects evolve a resistance to the natural pesticides engineered into Monsanto's plants, rendering the plants vulnerable to a new generation of super bugs.

For all of its appeal, utilitarian philosophy does have some serious drawbacks as an approach to business ethics. One problem is measuring the benefits, costs, and risks of a course of action. In the case of an oil company considering drilling in Alaska, how does one measure the potential harm done to the region's ecosystem? In the Monsanto example, how can one quantify the risk that genetically engineered crops might ultimately result in the evolution of super bugs that are resistant to the natural pesticide engineered into the crops? In general, utilitarian philosophers recognize that the measurement of benefits, costs, and risks is often not possible due to limited knowledge.

The second problem with utilitarianism is that the philosophy omits the consideration of justice. The action that produces the greatest good for the greatest number of people may result in the unjustified treatment of a minority. Such action cannot be ethical, precisely because it is unjust. For example, suppose that in the interests of keeping down health insurance costs, the government decides to screen people for the HIV virus and deny insurance coverage to those who are HIV positive. By reducing health costs, such action might produce significant benefits for a large number of people, but the action is unjust because it discriminates unfairly against a minority.

Kantian ethics are based on the philosophy of Immanuel Kant (1724–1804). **Kantian ethics** hold that people should be treated as ends and never purely as *means* to the ends of others. People are not instruments, like a machine. People have dignity and need to be respected as such. Employing people in sweatshops, making them work long hours for low pay in poor working conditions, is a violation of ethics, according to Kantian philosophy, because it treats people as mere cogs in a machine and not as conscious moral beings who have dignity. Although contemporary moral philosophers tend to view Kant's ethical philosophy as incomplete—for example, his system has no place for moral emotions or sentiments such as sympathy or caring—the notion that people should be respected and treated with dignity still resonates in the modern world.

RIGHTS THEORIES

Developed in the 20th century, **rights theories** recognize that human beings have fundamental rights and privileges that transcend national boundaries and cultures. Rights establish a minimum level of morally acceptable behavior. One well-known definition of a fundamental right construes it as something that takes precedence over or "trumps" a collective good. Thus, we might say that the right to free speech is a fundamental right that takes precedence over all but the most compelling collective goals and overrides, for example, the interest of the state in civil harmony or moral consensus.[37] Moral theorists argue that fundamental human rights form the basis for the *moral compass* that managers should navigate by when making decisions that have an ethical component. More precisely, they should not pursue actions that violate these rights.

The notion that there are fundamental rights that transcend national borders and cultures was the underlying motivation for the United Nations' **Universal Declaration of Human Rights,** which has been ratified by almost every country on the planet and lays down basic principles that should always be adhered to irrespective of the culture in which one is doing business.[38] Echoing Kantian ethics, Article 1 of this declaration states:

> Article 1: All human beings are born free and equal in dignity and rights. They are endowed with reason and conscience and should act towards one another in a spirit of brotherhood.

Article 23 of this declaration, which relates directly to employment, states:

> Everyone has the right to work, to free choice of employment, to just and favorable conditions of work, and to protection against unemployment.
> Everyone, without any discrimination, has the right to equal pay for equal work.
> Everyone who works has the right to just and favorable remuneration ensuring for himself and his family an existence worthy of human dignity, and supplemented, if necessary, by other means of social protection.
> Everyone has the right to form and to join trade unions for the protection of his interests.

Clearly, the rights embodied in Article 23 to "just and favorable work conditions," "equal pay for equal work," and remuneration that ensures an "existence worthy of human dignity" imply that it is unethical to employ child labor in sweatshop settings and pay less than subsistence wages, even if that happens to be common practice in some countries. These are fundamental human rights, which transcend national borders.

It is important to note that along with *rights* come *obligations*. Because we have the right to free speech, we are also obligated to make sure that we respect the free speech of others. The notion that people have obligations is stated in Article 29 of the Universal Declaration of Human Rights:

> Article 29: Everyone has duties to the community in which alone the free and full development of his personality is possible.

Within the framework of a theory of rights, certain people or institutions are obligated to provide benefits or services that secure the rights of others. Such obligations also fall upon more than one class of moral agent (a moral agent is any person or institution that is capable of moral action such as a government or corporation).

For example, to escape the high costs of toxic waste disposal in the West, in the late 1980s several firms shipped their waste in bulk to African nations, where it was disposed of at a much lower cost. In 1987, five European ships unloaded toxic waste containing dangerous poisons in Nigeria. Workers wearing sandals and shorts unloaded the barrels for $2.50 a day and placed them in a dirt lot in a residential area. They were not told about the contents of the barrels.[39] Who bears the obligation for protecting the rights of workers and residents to safety in a case like this? According to rights theorists, the obligation rests not on the shoulders of one moral agent, but on the shoulders of all moral agents whose actions might harm or contribute to the harm of the workers and residents. Thus, it was the obligation not just of the Nigerian government but also of the multinational firms that shipped the toxic waste to make sure it did no harm to residents and workers. In this case, both the government and the multinationals apparently failed to recognize their basic obligation to protect the fundamental human rights of others.

JUSTICE THEORIES

Justice theories focus on the attainment of a just distribution of economic goods and services. A **just distribution** is one that is considered fair and equitable. There is no one theory of justice, and several theories of justice conflict with each other in important ways.[40] Here we shall focus on one particular theory of justice that is both very influential and has important ethical implications, the theory attributed to philosopher John Rawls.[41] Rawls argues that all economic goods and services should be distributed equally except when an unequal distribution would work to everyone's advantage.

According to Rawls, valid principles of justice are those with which all persons would agree if they could freely and impartially consider the situation. Impartiality is guaranteed by a conceptual device that Rawls calls the *veil of ignorance*. Under the veil of ignorance, everyone is imagined to be ignorant of all of his or her particular characteristics, for example, race, sex, intelligence, nationality, family background, and special talents. Rawls then asks what system people would design under a veil of ignorance. Under these conditions, people would unanimously agree on two fundamental principles of justice.

The first principle is that each person be permitted the maximum amount of basic liberty compatible with a similar liberty for others. Rawls takes these to be political liberty (e.g., the right to vote), freedom of speech and assembly, liberty of conscience and freedom of thought, the freedom and right to hold personal property, and freedom from arbitrary arrest and seizure.

The second principle is that once equal basic liberty is assured, inequality in basic social goods—such as income and wealth distribution, and opportunities—is to be allowed *only* if such inequalities benefit everyone. Rawls accepts that inequalities can be just if the system that produces inequalities is to the advantage of everyone. More precisely, he formulates what he calls the *difference principle*, which is that inequalities are justified if they benefit the position of the least-advantaged person. So, for example, wide variations in income and wealth can be considered just if the market-based system that produces this unequal distribution also benefits the least-advantaged members of society. One can argue that a well-regulated, market-based economy and free trade, by promoting economic growth, benefit the least-advantaged members of society. In principle at least, the inequalities inherent in such systems are therefore just (in other words, the rising tide of wealth created by a market-based economy and free trade lifts all boats, even those of the most disadvantaged).

In the context of international business ethics, Rawls's theory creates an interesting perspective. Managers could ask themselves whether the policies they adopt in foreign operations would be considered just under Rawls's veil of ignorance. Is it just, for example, to pay foreign workers less than workers in the firm's home country? Rawls's theory would suggest it is, so long as the inequality benefits the least-advantaged members of the global society (which is what economic theory suggests). Alternatively, it is difficult to imagine that managers operating under a veil of ignorance would design a system where foreign employees were paid subsistence wages to work long hours in sweatshop conditions and where they were exposed to toxic materials. Such working conditions are clearly unjust in Rawls's framework, and therefore, it is unethical to adopt them. Similarly, operating under a veil of ignorance, most people would probably design a system that imparts some protection from environmental degradation to important global commons, such as the oceans, atmosphere, and tropical rain forests. To the extent that this is the case, it follows that it is unjust, and by extension unethical, for companies to pursue actions that contribute toward extensive degradation of these commons. Thus, Rawls's veil of ignorance is a conceptual tool that contributes to the moral compass that managers can use to help them navigate through difficult ethical dilemmas.

Ethical Decision Making

What, then, is the best way for managers in a multinational firm to make sure that ethical considerations figure into international business decisions? How do managers decide upon an ethical course of action when confronted with decisions pertaining to working conditions, human rights, corruption, and environmental pollution? From an ethical perspective, how do managers determine the moral obligations that flow from the power of a multinational corporation? In many cases, there are no easy answers to these questions, for many of the most vexing ethical problems arise because very real dilemmas are inherent in them and no correct action is obvious. Nevertheless, managers can and should do many things to make sure they adhere to basic ethical principles and routinely insert ethical issues into international business decisions.

Here we focus on five things that an international business and its managers can do to make sure ethical issues are considered in business decisions. These are to (1) favor hiring and promoting people with a well-grounded sense of personal ethics; (2) build an organizational culture that places a high value on ethical behavior; (3) make sure that leaders within the business not only articulate the rhetoric of ethical behavior but also act in a manner that is consistent with that rhetoric; (4) put decision-making processes in place that require people to consider the ethical dimension of business decisions; and (5) develop moral courage.

HIRING AND PROMOTION

It seems obvious that businesses should strive to hire people who have a strong sense of personal ethics and would not engage in unethical or illegal behavior. Similarly, you would not expect a business to promote people whose behavior does not match generally accepted ethical standards—you might expect the business to fire them. However, actually doing so is very difficult. How do you know that someone has a poor sense of personal ethics? In our society, we have an incentive to hide a lack of personal ethics from public view. Once people realize you are unethical, they will no longer trust you.

Is there anything businesses can do to make sure they do not hire people who subsequently turn out to have poor personal ethics, particularly given that people have an incentive to hide this from public view (indeed, the unethical person may lie about his or her nature)? Businesses can give potential employees psychological tests to try to discern their ethical predisposition, and they can check with prior employers regarding someone's reputation (e.g., by asking for letters of reference and talking to people who have worked with the prospective employee). The latter is common and does influence the hiring process. Promoting people who have displayed poor ethics should not occur in a company where the organization culture values the need for ethical behavior and where leaders act accordingly.

Not only should businesses strive to identify and hire people with a strong sense of personal ethics, but it also is in the interests of prospective employees to find out as much as they can about the ethical climate in an organization. Who wants to work at a multinational such as Enron, which ultimately entered bankruptcy because unethical executives had established risky partnerships that were hidden from public view and that existed in part to enrich those same executives? Table 4.1 lists some questions job seekers might want to ask a prospective employer.

ORGANIZATION CULTURE AND LEADERSHIP

To foster ethical behavior, businesses need to build an organization culture that values ethical behavior. Three things are particularly important in building an organization culture that emphasizes ethical behavior. First, the businesses must explicitly articulate values that emphasize ethical behavior. Many companies now do this by drafting a **code of ethics,** which is a formal statement of the ethical priorities a business adheres to. Often, the code of ethics draws heavily upon documents such as the UN Universal Declaration of Human Rights, which itself is grounded in Kantian and rights-based theories of moral philosophy. Others have incorporated ethical statements into documents that articulate the values or mission of the business. For example, the food and consumer products multinational Unilever has a code of ethics that includes the following points:[42]

> **Employees:** Unilever is committed to diversity in a working environment where there is mutual trust and respect and where everyone feels responsible for the performance and reputation of our company. We will recruit, employ, and promote employees on the sole

TABLE 4.1

A Job Seeker's Ethics Audit

Source: Linda K. Trevino, chair of the Department of Management and Organization, Smeal College of Business, Pennsylvania State University. Reported in K. Maher, "Career Journal. Wanted: Ethical Employer," *The Wall Street Journal*, July 9, 2002, p. B1.

Some probing questions to ask about a prospective employer:
1. Is there a formal code of ethics? How widely is it distributed? Is it reinforced in other formal ways such as through decision-making systems?
2. Are workers at all levels trained in ethical decision making? Are they also encouraged to take responsibility for their behavior or to question authority when asked to do something they consider wrong?
3. Do employees have formal channels available to make their concerns known confidentially? Is there a formal committee high in the organization that considers ethical issues?
4. Is misconduct disciplined swiftly and justly within the organization?
5. Is integrity emphasized to new employees?
6. How are senior managers perceived by subordinates in terms of their integrity? How do such leaders model ethical behavior?

basis of the qualifications and abilities needed for the work to be performed. We are committed to safe and healthy working conditions for all employees. We will not use any form of forced, compulsory, or child labor. We are committed to working with employees to develop and enhance each individual's skills and capabilities. We respect the dignity of the individual and the right of employees to freedom of association. We will maintain good communications with employees through company-based information and consultation procedures.

Business Integrity: Unilever does not give or receive, whether directly or indirectly, bribes or other improper advantages for business or financial gain. No employee may offer, give, or receive any gift or payment which is, or may be construed as being, a bribe. Any demand for, or offer of, a bribe must be rejected immediately and reported to management. Unilever accounting records and supporting documents must accurately describe and reflect the nature of the underlying transactions. No undisclosed or unrecorded account, fund, or asset will be established or maintained.

It is clear from these principles that, among other things, Unilever will not tolerate substandard working conditions, use child labor, or give bribes under any circumstances. Note also the reference to respecting the dignity of employees, a statement that is grounded in Kantian ethics. Unilever's principles send a very clear message about appropriate ethics to managers and employees.

Having articulated values in a code of ethics or some other document, leaders in the business must give life and meaning to those words by repeatedly emphasizing their importance *and then acting on them*. This means using every relevant opportunity to stress the importance of business ethics and making sure that key business decisions not only make good economic sense but also are ethical. Many companies have gone a step further, hiring independent auditors to make sure they are behaving in a manner consistent with their ethical codes. Nike, for example, has hired independent auditors to make sure that the company's subcontractors are living up to Nike's code of conduct.

Finally, building an organization culture that places a high value on ethical behavior requires incentive and reward systems, including promotions that reward people who engage in ethical behavior and sanction those who do not. At General Electric, for example, the former CEO Jack Welch has described how he reviewed the performance of managers, dividing them into several different groups. These included overperformers who displayed the right values and were singled out for advancement and bonuses and overperformers who displayed the wrong values and were let go. Welch was not willing to tolerate leaders within the company who did not act in accordance with the central values of the company, even if they were in all other respects skilled managers.[43]

DECISION-MAKING PROCESSES

In addition to establishing the right kind of ethical culture in an organization, businesspeople must be able to think through the ethical implications of decisions in a systematic way. To do this, they need a moral compass, and both rights theories and Rawls's theory of justice help to provide such a compass. Beyond these theories, some experts on ethics have proposed a straightforward practical guide—or ethical algorithm—to determine whether a decision is ethical.[44] According to these experts, a decision is acceptable on ethical grounds if a businessperson can answer yes to each of these questions:

- Does my decision fall within the accepted values or standards that typically apply in the organizational environment (as articulated in a code of ethics or some other corporate statement)?
- Am I willing to see the decision communicated to all stakeholders affected by it—for example, by having it reported in newspapers or on television?
- Would the people with whom I have a significant personal relationship, such as family members, friends, or even managers in other businesses, approve of the decision?

Others have recommended a five-step process to think through ethical problems (this is another example of an ethical algorithm).[45] In step 1, businesspeople should identify which stakeholders a decision would affect and in what ways. A firm's **stakeholders** are individuals or groups that have an interest, claim, or stake in the company, what it does, and how well it performs.[46] They can be divided into internal stakeholders and external stakeholders. **Internal stakeholders** are individuals or groups who work for or own the business. They include all employees, the board of directors, and stockholders. **External stakeholders** are all other individuals and groups that have some claim on the firm. Typically, this group comprises customers, suppliers, lenders, governments, unions, local communities and the general public.

All stakeholders are in an exchange relationship with the company. Each stakeholder group supplies the organization with important resources (or contributions), and in exchange each expects its interests to be satisfied (by inducements).[47] For example, employees provide labor, skills, knowledge, and time and in exchange expect commensurate income, job satisfaction, job security, and good working conditions. Customers provide a company with its revenues and in exchange they want quality products that represent value for money. Communities provide businesses with local infrastructure and in exchange they want businesses that are responsible citizens and seek some assurance that the quality of life will be improved as a result of the business firm's existence.

Stakeholder analysis involves a certain amount of what has been called *moral imagination*.[48] This means standing in the shoes of a stakeholder and asking how a proposed decision might impact that stakeholder. For example, when considering outsourcing to subcontractors, managers might need to ask themselves how it might feel to be working under substandard health conditions for long hours.

Step 2 involves judging the ethics of the proposed strategic decision, given the information gained in step 1. Managers need to determine whether a proposed decision would violate the *fundamental rights* of any stakeholders. For example, we might argue that the right to information about health risks in the workplace is a fundamental entitlement of employees. Similarly, the right to know about potentially dangerous features of a product is a fundamental entitlement of customers (something tobacco companies violated when they did not reveal to their customers what they knew about the health risks of smoking). Managers might also want to ask themselves whether they would allow the proposed strategic decision if they were designing a system under Rawls's veil of ignorance. For example, if the issue under consideration was whether to outsource work to a subcontractor with low pay and poor working conditions, managers might want to ask themselves whether they would allow for such action if they were considering it under a veil of ignorance, where they themselves might ultimately be the ones to work for the subcontractor.

The judgment at this stage should be guided by various moral principles that should not be violated. The principles might be those articulated in a corporate code of ethics or other company documents. In addition, certain moral principles that we have adopted as members of society—for instance, the prohibition on stealing—should not be violated. The judgment at this stage will also be guided by the decision rule that is chosen to assess the proposed strategic decision. Although most businesses stress the decision rule of maximizing long-run profitability, it should be applied subject to the constraint that no moral principles are violated—that the business behaves in an ethical manner.

Step 3 requires managers to establish moral intent. This means the business must resolve to place moral concerns ahead of other concerns in cases where either the fundamental rights of stakeholders or key moral principles have been violated. At this stage, input from top management might be particularly valuable. Without the proactive encouragement of top managers, middle-level managers might tend to place the narrow economic interests of the company before the interests of stakeholders. They might do so in the (usually erroneous) belief that top managers favor such an approach.

Step 4 requires the company to engage in ethical behavior. Step 5 requires the business to audit its decisions, reviewing them to make sure they were consistent with ethical principles, such as those stated in the company's code of ethics. This final step is critical and often overlooked. Without auditing past decisions, businesspeople may not know if their decision process is working and if changes should be made to ensure greater compliance with a code of ethics.

ETHICS OFFICERS

To make sure that a business behaves in an ethical manner, a number of firms now have ethics officers. These individuals are responsible for making sure that all employees are trained to be ethically aware, that ethical considerations enter the business decision-making process, and that the company's code of ethics is followed. Ethics officers may also be responsible for auditing decisions to make sure they are consistent with this code. In many businesses, ethics officers act as an internal ombudsperson with responsibility for handling confidential inquiries from employees, investigating complaints from employees or others, reporting findings, and making recommendations for change.

For example, United Technologies, a multinational aerospace company with worldwide revenues of more than $30 billion, has had a formal code of ethics since 1990.[49] The company has some 160 business practice officers (its name for ethics officers) who are responsible for making sure the code is followed. United Technologies also established an ombudsperson program in 1986 that lets employees inquire anonymously about ethics issues. The program has received some 56,000 inquiries since 1986, and ombudspeople have handled 8,000 cases.

MORAL COURAGE

Finally, it is important to recognize that employees in an international business may need significant *moral courage*. Moral courage enables managers to walk away from a decision that is profitable but unethical. Moral courage gives an employee the strength to say no to a superior who instructs her to pursue actions that are unethical. Moral courage gives employees the integrity to go public to the media and blow the whistle on persistent unethical behavior in a company. Moral courage does not come easily; there are well-known cases where individuals have lost their jobs because they blew the whistle on corporate behaviors they thought unethical, telling the media about what was occurring.[50]

However, companies can strengthen the moral courage of employees by committing themselves to not retaliate against employees who exercise moral courage, say no to superiors, or otherwise complain about unethical actions. For example, consider the following extract from Unilever's code of ethics:

> Any breaches of the Code must be reported in accordance with the procedures specified by the Joint Secretaries. The Board of Unilever will not criticize management for any loss of business resulting from adherence to these principles and other mandatory policies and instructions. The Board of Unilever expects employees to bring to their attention, or to that of senior management, any breach or suspected breach of these principles. Provision has been made for employees to be able to report in confidence and no employee will suffer as a consequence of doing so.[51]

This statement gives permission to employees to exercise moral courage. Companies can also set up ethics hotlines, which allow employees to anonymously register a complaint with a corporate ethics officer.

SUMMARY OF DECISION-MAKING STEPS

All the steps discussed here—hiring and promoting people based upon ethical considerations as well as more traditional metrics of performance, establishing an ethical culture in the organization, instituting ethical decision-making processes, appointing ethics officers, and creating an environment that facilitates moral courage—can help ensure that managers are cognizant of the ethical implications of business decisions and do not violate basic ethical prescripts. At the same time, it must be recognized that not all ethical dilemmas have a clean and obvious solution—that is why they are dilemmas. There are clearly things that international businesses should not do and there are things that they should do, but there are also actions that present managers with true dilemmas. In these cases, a premium is placed on managers' ability to make sense out of complex situations and make balanced decisions that are as just as possible.

CHAPTER SUMMARY

This chapter has discussed the source and nature of ethical issues in international businesses, the different philosophical approaches to business ethics, and the steps managers can take to ensure that ethical issues are respected in international business decisions. The chapter made these points:

1. The term *ethics* refers to accepted principles of right or wrong that govern the conduct of a person, the members of a profession, or the actions of an organization. Business ethics are the accepted principles of right or wrong governing the conduct of businesspeople, and an ethical strategy is one that does not violate these accepted principles.
2. Ethical issues and dilemmas in international business are rooted in the variations among political systems, law, economic development, and culture from nation to nation.
3. The most common ethical issues in international business involve employment practices, human rights, environmental regulations, corruption, and the moral obligation of multinational corporations.
4. Ethical dilemmas are situations in which none of the available alternatives seems ethically acceptable.
5. Unethical behavior is rooted in poor personal ethics, the psychological and geographical distances of a foreign subsidiary from the home office, a failure to incorporate ethical issues into strategic and operational decision making, a dysfunctional culture, and failure of leaders to act in an ethical manner.
6. Moral philosophers contend that approaches to business ethics such as the Friedman doctrine, cultural relativism, the righteous moralist, and the naive immoralist are unsatisfactory in important ways.
7. The Friedman doctrine states that the only social responsibility of business is to increase profits, as long as the company stays within the

rules of law. Cultural relativism contends that one should adopt the ethics of the culture in which one is doing business. The righteous moralist monolithically applies home-country ethics to a foreign situation, while the naive immoralist believes that if a manager of a multinational sees that firms from other nations are not following ethical norms in a host nation, that manager should not either.

8. Utilitarian approaches to ethics hold that the moral worth of actions or practices is determined by their consequences, and the best decisions are those that produce the greatest good for the greatest number of people.
9. Kantian ethics state that people should be treated as ends and never purely as *means* to the ends of others. People are not instruments, like a machine. People have dignity and need to be respected as such.
10. Rights theories recognize that human beings have fundamental rights and privileges that transcend national boundaries and cultures. These rights establish a minimum level of morally acceptable behavior.
11. The concept of justice developed by John Rawls suggests that a decision is just and ethical if people would allow for it when designing a social system under a veil of ignorance.
12. To make sure that ethical issues are considered in international business decisions, managers should (*a*) favor hiring and promoting people with a well-grounded sense of personal ethics; (*b*) build an organization culture that places a high value on ethical behavior; (*c*) make sure that leaders within the business not only articulate the rhetoric of ethical behavior but also act in a manner that is consistent with that rhetoric; (*d*) put decision-making processes in place that require people to consider the ethical dimension of business decisions; and (*e*) be morally courageous and encourage others to do the same.

Critical Thinking and Discussion Questions

1. A visiting American executive finds that a foreign subsidiary in a poor nation has hired a 12-year-old girl to work on a factory floor, in violation of the company's prohibition on child labor. He tells the local manager to replace the child and tell her to go back to school. The local manager tells the American executive that the child is an orphan with no other means of support, and she will probably become a street child if she is denied work. What should the American executive do?
2. Drawing upon John Rawls's concept of the veil of ignorance, develop an ethical code that will (*a*) guide the decisions of a large oil multinational toward environmental protection, and (*b*) influence the policies of a clothing company regarding outsourcing manufacturing process.
3. Under what conditions is it ethically defensible to outsource production to the developing world where labor costs are lower when such actions also involve laying off long-term employees in the firm's home country?
4. Are facilitating payments ethical?
5. A manager from a developing country is overseeing a multinational's operations in a country where drug trafficking and lawlessness are rife. One day, a representative of a local "big man" approaches the manager and asks for a "donation" to help the "big man" provide housing for the poor. The representative tells the manager that in return for the donation, the "big man" will make sure that the manager has a productive stay in his country. No threats are made, but the manager is well aware that the "big man" heads a criminal organization that is engaged in drug trafficking. He also knows that that the big man does indeed help the poor in the run-down neighborhood of the city where he was born. What should the manager do?
6. Reread the Management Focus feature on Unocal and answer the following questions:
   a. Was it ethical for Unocal to enter into a partnership with a brutal military dictatorship for financial gain?
   b. What actions could Unocal have taken, short of not investing at all, to safeguard the human rights of people impacted by the gas pipeline project?

Research Task globalEDGE http://globalEDGE.msu.edu

Use the globalEDGE™ site to complete the following exercises:

1. Promoting respect for universal human rights is a central dimension of many countries' foreign policy. As history has shown, human rights abuses are an important concern worldwide. Some countries are more ready to work with other governments and civil society organizations to prevent abuses of power. Begun in 1977, the annual Country Reports on Human Rights Practices are designed to assess the state of democracy and human rights around the world, call attention to violations, and—where needed—prompt needed changes in U.S. policies toward particular countries. Find the annual Country Reports on Human Rights Practices and provide information on how the reports are prepared.
2. The level of perceived corruption varies from culture to culture. The *Corruption Perceptions Index (CPI)* is a comparative assessment of a country's integrity performance based on research done in Germany. Provide a description of this index and its ranking. Identify the five countries with the lowest as well as the highest CPI scores. Do you notice any similarities or differences in each group of five countries?

CLOSING CASE

Google in China

Google, the fast growing Internet search engine company, was established with a clear mission in mind: to organize the world's information and make it universally accessible and useful. Google has built a highly profitable advertising business on the back of its search engine, which is by far the most widely used in the world. Under the pay-per-click business model, advertisers pay Google every time a user of its search engine clicks on one of the paid links typically listed on the right hand side of Google's results page.

Google has long operated with the mantra "don't be evil!" When this phrase was originally formulated, the central message was that Google should never compromise the integrity of its search results. For example, Google decided not to let commercial considerations bias its ranking. This is why paid links are not included in its main search results, but listed on the right hand side of the results page. The mantra "don't be evil," however, has become more than that at Google; it has become a central organizing principle of the company and an ethical touchstone by which managers judge all of its strategic decisions.

Google's mission and mantra raised hopes among human rights activities that the search engine would be an unstoppable tool for circumventing government censorship, democratizing information, and allowing people in heavily censored societies to gain access to information that their governments were trying to suppress, including the largest country on earth, China.

Google began a Chinese language service in 2000, although the service was operated from the United States. In 2002, Chinese authorities blocked the site. Would-be users of Google's search engine were directed to a Chinese rival. The blocking took Google's managers totally by surprise. Reportedly, co-founder Sergey Brin immediately ordered half a dozen books on China and quickly read them in an effort to understand this vast country. Two weeks later, for reasons that have never been made clear, Google's service was restored. Google said that it did not change anything about its service, but Chinese users soon found that they could not access politically sensitive sites that appeared in Google's search results, suggesting that the government was censoring more aggressively. (The Chinese government has essentially erected a giant firewall between the Internet in China and the rest of the world, allowing its censors to block sites outside of China that are deemed subversive.)

By late 2004, it was clear to Google that China was a strategically important market. To exploit the opportunities that China offered, however, the company realized it would have to establish operations in China, including its own computer servers and a Chinese home page. Serving Chinese users from the United States was too slow, and the service was badly degraded by the censorship imposed. This created a dilemma for the company given the "don't be evil" mantra. Once it established Chinese operations, it would be subject to Chinese regulations, including those censoring information. For perhaps 18 months, senior managers inside the company debated the pros and cons of entering China directly, as opposed to serving the market from its U.S. site. Ultimately, they decided that the opportunity was too large to ignore. With over 100 million users, and that number growing fast, China promised to become the largest Internet market in the world and a major source of advertising revenue for Google. Moreover, Google was at a competitive disadvantage relative to its U.S. rivals, Yahoo and Microsoft's MSN, which had already established operations in China, and relative to China's homegrown company, Baidu, which leads the market for Internet search in China (in 2006 Baidu had around 40 percent of the market for search in China, compared to Google's 30 percent share).

In mid-2005, Google established a direct sales presence in China. In January 2006, Google rolled out its Chinese home page, which is hosted on servers based in China and maintained by Chinese employees in Beijing and Shanghai. Upon launch, Google stated that its objective was to give Chinese users "the greatest amount of information possible." It was immediately apparent that this was not the same as "access to all information." In accordance with Chinese regulations, Google had decided to engage in self-censorship, excluding results on such politically sensitive topics as democratic reform, Taiwanese independence, the banned Falun Gong movement, and references to the notorious Tiananmen Square massacre of democratic protestors that occurred in 1989. Human rights activists quickly protested, arguing that Google had abandoned its principles in order to make greater profits. For its part, Google's managers claimed that it was better to give Chinese users access to a limited amount of information, than to none at all, or to serve the market from the United States and allow the government to continue proactively censoring its search results, which would result in a badly degraded service. Sergey Brin justified the Chinese decision by saying that "it will be better for Chinese web users, because ultimately they will get more information, though not quite all of it." Moreover, Google argued that it was the only search engine in China that let users know if search results had been censored (which is done by the inclusion of a bullet at the bottom of the page indicating censorship).[52]

Case Discussion Questions

1. What philosophical principle did Google's managers adopt when deciding that the benefits of operating in China outweighed the costs?
2. Do you think that Google should have entered China and engaged in self-censorship, given the company's long-standing mantra "Don't be evil"? Is it better to engage in self-censorship than have the government censor for you?
3. If all foreign search engine companies declined to invest directly in China due to concerns over censorship, what do you think the results would be? Who would benefit most from this action? Who would lose the most?

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Nike: The Sweatshop Debate

INTRODUCTION

Nike is in many ways the quintessential global corporation. Established in 1972 by former University of Oregon track star Phil Knight, Nike is now one of the leading marketers of athletic shoes and apparel on the planet. In 2006 the company had $15 billion in annual revenues and sold its products in some 140 countries. Nike does not do any manufacturing. Rather, it designs and markets its products, while contracting for their manufacture from a global network of 600 factories scattered around the globe that employ some 650,000 people.[1] This huge corporation has made founder Phil Knight into one of the richest people in America. Nike's marketing phrase, "Just Do It!" has become as recognizable in popular culture as its "swoosh" logo or the faces of its celebrity sponsors, such as Michael Jordan and Tiger Woods.

For all of its successes, the company was dogged for more than a decade by repeated and persistent accusations that its products were made in "sweatshops" where workers, many of them children, slaved away in hazardous conditions for below-subsistence wages. Nike's wealth, its detractors claimed, was built upon the backs of the world's poor. For many, Nike had become a symbol of the evils of globalization—a rich Western corporation exploiting the world's poor to provide expensive shoes and apparel to the pampered consumers of the developed world. Nike's "Niketown" stores became standard targets for antiglobalization protestors. Several nongovernmental organizations, such as San Francisco–based Global Exchange, a human rights organization dedicated to promoting environmental, political, and social justice around the world, targeted Nike for repeated criticism and protests.[2] News organizations such as CBS's *48 Hours* hosted by Dan Rather ran exposés on working conditions in foreign factories that supply Nike. Students on the campuses of several major U.S. universities with which Nike has lucrative sponsorship deals protested against the ties, citing Nike's use of sweatshop labor.

For its part, Nike has taken many steps to try to counter the protests. Yes, it admits, there have been problems in some overseas factories. But the company has signaled a commitment to improving working conditions. It requires that foreign subcontractors meet minimum thresholds for working conditions and pay. It has arranged for factories to be examined by independent auditors. It has terminated contracts with factories that do not comply with its standards. But for all this effort, the company continues to be a target of protests and a symbol of dissent.

THE CASE AGAINST NIKE

Typical of the exposés against Nike was a CBS *48 Hours* news report that aired on October 17, 1996.[3] Reporter Roberta Basin visited a Nike factory in Vietnam. With a shot of the factory, her commentary begin by saying that

> The signs are everywhere of an American invasion in search of cheap labor. Millions of people who are literate, disciplined, and desperate for jobs. This is Nike Town near what use to be called Saigon, one of four factories Nike doesn't own but subcontracts to make a million shoes a month. It takes 25,000 workers, mostly young women, to "Just Do It."
>
> But the workers here don't share in Nike's huge profits. They work six days a week for only $40 a month, just 20 cents an hour.

Baskin interviews one of the workers in the factory, a young woman named Lap. Baskin tells the listener:

> Her basic wage, even as sewing team leader, still doesn't amount to the minimum wage. . . . She's down to 85 pounds. Like most of the young women who make shoes, she has little choice but to accept the low wages and long hours. Nike says that it requires all subcontractors to obey local laws; but Lap has already put in much more overtime than the annual legal limit: 200 hours.

Baskin then asks Lap what would happen if she wanted to leave. If she were sick or had something she needed to take care of such as a sick relative, could she leave the factory? Through a translator, Lap replies:

> It is not possible if you haven't made enough shoes. You have to meet the quota before you can go home.

The clear implication of the story was that Nike was at fault here for allowing such working conditions to persist in the Vietnam factory, which, incidentally, was owned by a Korean company.

Another example of an attack on Nike's subcontracting practices came in June 1996 from Made in the USA, a foundation largely financed by labor unions and domestic apparel manufacturers that oppose free trade with low-wage countries. According to Joel Joseph, chairman of the foundation, a popular line of high-priced Nike sneakers, the "Air Jordans," were put together made by 11-year-olds in Indonesia making 14 cents per hour. A Nike spokeswoman, Donna Gibbs, countered that this statement was

[1] From Nike's corporate Web site at www.nikebiz.com.
[2] www.globalexchange.org.
[3] "Boycott Nike" CBS News, *48 Hours*, October 17, 1996.

in fact false. According to Gibbs, the average worker made 240,000 rupiah ($103) a month working a maximum 54-hour week, or about 45 cents per hour. Moreover, Gibbs noted that Nike had staff members in each factory monitoring conditions to make sure that they obeyed local minimum wage and child labor laws.[4]

Another example of the criticism against Nike is the following extract from a newsletter published by Global Exchange:[5]

> During the 1970s, most Nike shoes were made in South Korea and Taiwan. When workers there gained new freedom to organize and wages began to rise, Nike looked for "greener pastures." It found them in Indonesia and China, where Nike started producing in the 1980s, and most recently in Vietnam. The majority of Nike shoes are made in Indonesia and China, countries with governments that prohibit independent unions and set the minimum wage at rock bottom. The Indonesian government admits that the minimum wage there does not provide enough to supply the basic needs of one person, let alone a family. In early 1997 the entry-level wage was a miserable $2.46 a day. Labor groups estimate that a livable wage in Indonesia is about $4.00 a day.
>
> In Vietnam the pay is even less—20 cents an hour, or a mere $1.60 a day. But in urban Vietnam, three simple meals cost about $2.10 a day, and then of course there is rent, transportation, clothing, health care, and much more. According to Thuyen Nguyen of Vietnam Labor Watch, a living wage in Vietnam is at least $3 a day.

In another attack on Nike's practices, in September 1997 Global Exchange published a report on working conditions in four Nike and Reebok subcontractors in Southern China.[6] Global Exchange, in conjunction with two Hong Kong human rights groups, had interviewed workers at the factories in 1995 and again in 1997. According to Global Exchange, in one factory, owned by a Korean subcontractor for Nike, workers as young as 13 earning as little as 10 cents an hour toiled up to 17 hours daily in enforced silence. Talking during work was not allowed, with violators fined $1.20 to $3.60 according to the report. The practices were in violation of Chinese labor law, which states that no child under 16 may work in a factory, and the Chinese minimum wage requirement of $1.90 for an eight-hour day. Nike condemned the study as "erroneous," stating that it incorrectly stated the wages of workers and made irresponsible accusations.

Global Exchange, however, continued to be a major thorn in Nike's side. In November 1997, the organization obtained and then leaked a confidential report by Ernst & Young of an audit that Nike had commissioned of a factory in Vietnam owned by a Nike subcontractor.[7] The factory had 9,200 workers and made 400,000 pairs of shoes a month. The Ernst & Young report painted a dismal picture of thousands of young women, most under age 25, laboring 10½ hours a day, six days a week, in excessive heat and noise and in foul air, for slightly more than $10 a week. The report also found that workers with skin or breathing problems had not been transferred to departments free of chemicals and that more than half the workers who dealt with dangerous chemicals did not wear protective masks or gloves. It claimed workers were exposed to carcinogens that exceeded local legal standards by 177 times in parts of the plant and that 77 percent of the employees suffered from respiratory problems.

Put on the defensive yet again, Nike called a news conference and pointed out that it had commissioned the report, and had acted on it.[8] The company stated that it had formulated an action plan to deal with the problems cited in the report, and had slashed overtime, improved safety and ventilation, and reduced the use of toxic chemicals. The company also asserted that the report showed that its internal monitoring system had performed exactly as it should have. According to one spokesman, "This shows our system of monitoring works. . . . We have uncovered these issues clearly before anyone else, and we have moved fairly expeditiously to correct them."

NIKE'S RESPONSES

Unaccustomed to playing defense, over the years Nike formulated a number of strategies and tactics to deal with the problems of subcontractors' working conditions and pay. In 1996, Nike hired one-time U.S. Ambassador to the United Nations and former Atlanta Mayor and Congressional representative Andrew Young to assess working conditions in subcontractors' plants around the world. After completing a two-week tour that involved inspecting 15 factories in three countries, Young released a mildly critical report of Nike in mid-1997. He informed Nike it was doing a good job in treating workers, though it should do better. According to Young, he did not see

> sweatshops, or hostile conditions . . . I saw crowded dorms . . . but the workers were eating at least two meals a day on the job and making what I was told were subsistence wages in those cultures.[9]

Young was widely criticized by human rights and labor groups for not taking his own translators and for

[4]D. Jones, "Critics Tie Sweatshop Sneakers to 'Air Jordan,'" *USA Today,* June 6, 1996, p. 1B.
[5]Global Exchange Special Report: "Nike Just Don't Do It," http://www.globalexchange.org/education/publications/newsltr6.97p2.html#nike.
[6] V. Dobnik, "Chinese Workers Abused Making Nikes, Reeboks," *Seattle Times*, September 21, 1997, p. A4.
[7]S. Greenhouse, "Nike Shoeplant in Vietnam Is Called Unsafe for Workers," *The New York Times,* November 8, 1997.
[8]Greenhouse, "Nike Shoeplant in Vietnam Is Called Unsafe for Workers."
[9]Quoted in V. Dobnik, "Chinese Workers Abused Making Nikes, Reeboks," *Seattle Times,* September 21, 1997, p. A4.

doing slipshod inspections, an assertion he repeatedly denied.

In 1996, Nike joined a presidential task force designed to find a way of banishing sweatshops in the shoe and clothing industries. The task force included industry leaders such as Nike, representatives from human rights groups, and labor leaders. In April 1997, the task force announced a workers' rights agreement that U.S. companies could accept when manufacturing abroad. The accord limited the workweek to 60 hours and called for paying at least the local minimum wage in foreign factories. The task force also agreed to establish an independent monitoring association—later named the Fair Labor Association (FLA)—to assess whether companies are abiding by the code.[10]

The FLA now includes among its members the Lawyers Committee for Human Rights, the National Council of Churches, the International Labor Rights Fund, some 135 universities (universities have extensive licensing agreements with sports apparel companies such as Nike), and companies such as Nike, Reebok, and Levi Strauss.

In early 1997, Nike also began to commission independent organizations such as Ernst & Young to audit its subcontractors' factories. In September 1997, Nike tried to show its critics that it was involved in more than just a public relations exercise when it terminated its relationship with four Indonesian subcontractors, stating that these subcontractors had refused to comply with the company's standard for wage levels and working conditions. Nike identified one of the subcontractors, Seyon, which manufactured specialty sports gloves for Nike. Nike said that Seyon refused to meet a 10.7 percent increase in the monthly wage, to $70.30, declared by the Indonesian government in April 1997.[11]

On May 12, 1998, in a speech given at the National Press Club, Phil Knight spelled out in detail a series of initiatives designed to improve working conditions for the 500,000 people that make products for Nike as subcontractors.[12] Among the initiatives Knight highlighted were the following:

- We have effectively changed our minimum age limits from the ILO (International Labor Organization) standards of 15 in most countries and 14 in developing countries to 18 in all footwear manufacturing and 16 in all other types of manufacturing (apparel, accessories and equipment). Existing workers legally employed under the former limits were grand-fathered into the new requirements.
- During the past 13 months we have moved to a 100 percent factory audit scheme, where every Nike contract factory will receive an annual check by PricewaterhouseCoopers teams who are specially trained on our Code of Conduct Owner's Manual and audit/monitoring procedures. To date they have performed about 300 such monitoring visits. In a few instances in apparel factories they have found workers under our age standards. Those factories have been required to raise their standards to 17 years of age, to require three documents certifying age, and to redouble their efforts to ensure workers meet those standards through interviews and records checks.
- Our goal was to ensure workers around the globe are protected by requiring factories to have no workers exposed to levels above those mandated by the permissible exposure limits (PELs) for chemicals prescribed in the OSHA indoor air quality standards.[13]

The business press applauded these moves, but Nike's long-term adversaries in the debate over the use of foreign labor greeted them skeptically. While conceding that's Nike's policies were an improvement, one critic writing in *The New York Times* noted that

> Mr. Knight's child labor initiative is . . . a smokescreen. Child labor has not been a big problem with Nike, and Philip Knight knows that better than anyone. But public relations is public relations. So he announces that he's not going to let the factories hire kids, and suddenly that's the headline.
>
> Mr. Knight is like a three-card monte player. You have to keep a close eye on him at all times.
>
> The biggest problem with Nike is that its overseas workers make wretched, below-subsistence wages. It's not the minimum age that needs raising, it's the minimum wage. Most of the workers in Nike factories in China and Vietnam make less than $2 a day, well below the subsistence levels in those countries. In Indonesia the pay is less than $1 a day.
>
> The company's current strategy is to reshape its public image while doing as little as possible for the workers. Does anyone think it was an accident that Nike set up shop in human rights sinkholes, where labor organizing was viewed as a criminal activity and deeply impoverished workers were willing, even eager, to take their places on assembly lines and work for next to nothing?[14]

Other critics question the value of Nike's auditors, PricewaterhouseCoopers (PwC). Dara O'Rourke, an assistant professor at MIT, followed the PwC auditors

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[10]W. Bounds and H. Stout, "Sweatshop Pact: Good Fit or Threadbare?" *The Wall Street Journal,* April 10, 1997, p. A2.

[11]"Nike Gives Four Factories the Boot," *Los Angeles Times,* September 23, 1997, p. 20.

[12]Archived at http://www.nikebiz.com/labor/speech_trans.shtml.

[13]OSHA is the United States Occupational Safety and Health Agency.

[14]B. Herbet, "Nike Blinks," *The New York Times,* May 21, 1998.

around several factories in China, Korea, and Vietnam. He concluded that although the auditors found minor violations of labor laws and codes of conduct, they missed major labor practice issues including hazardous working conditions, violations of overtime laws, and violation of wage laws. The problem, according to O'Rourke, was that the auditors had limited training, and relied on factory managers for data and to set up interviews with workers, all of which were performed in the factories. The auditors, in other words, were getting an incomplete and somewhat sanitized view of conditions in the factory.[15]

THE CONTROVERSY CONTINUES

Fueled perhaps by the unforgiving criticisms of Nike that continued after Phil Knight's May 1998 speech, a wave of protests against Nike occurred on many university campuses beginning in 1998 and continuing into 2001. The moving force behind the protests was the United Students Against Sweatshops (USAS). The USAS argued that the Fair Labor Association (FLA), which grew out of the Presidential task force on sweatshops, was an industry tool, and not a truly independent auditor of foreign factories. The USAS set up an alternative independent auditing organization, the Workers Rights Consortium (WRC), which they charged with auditing factories that produce products under collegiate licensing programs (Nike is a high-profile supplier of products under these programs). The WRC is backed, and partly funded, by labor unions and refuses to cooperate with companies, arguing that doing so would jeopardize its independence.

By mid-2000, the WRC had persuaded some 48 universities to join the WRC, including all nine campuses of the University of California systems, the University of Michigan, and the University of Oregon, Phil Knight's alma mater. When Knight heard that the University of Oregon would join the WRC, as opposed to the FLA, he withdrew a planned $30 million donation to the University.[16] Despite Knight's opposition, in November 2000 another major university in the northwest, the University of Washington, announced that it too would join the WRC, although it would also retain its membership in the FLA.[17]

Nike continued to push forward with its own initiatives, updating progress on its Web site. In April 2000, in response to accusations that it was still hiding conditions, it announced that it would release the complete reports of all independent audits of its subcontractors' plants. Global Exchange continued to criticize the company, arguing in mid-2001 that the company was not living up to Phil Knight's 1998 promises and that it was intimidating workers from speaking out about abuses.[18]

Case Discussion Questions

1. Should Nike be held responsible for working conditions in foreign factories that it does not own, but where subcontractors make products for Nike?
2. What labor standards regarding safety, working conditions, overtime, and the like, should Nike hold foreign factories to: those prevailing in that country or those prevailing in the United States?
3. In Indonesia, an income of $2.28 a day, the base pay of Nike factory workers, is double the daily income of about half the working population. Half of all adults in Indonesia are farmers, who receive less than $1 a day. Given these national standards, is it appropriate to criticize Nike for the low pay rates of its subcontractors in Indonesia?[19]
4. Could Nike have handled the negative publicity over sweatshops better? What might it have done differently, not just from a public relations perspective but also from a policy perspective?
5. Do you think Nike needs to make any changes to its current policy? If so what? Should Nike make changes even if they hinder the ability of the company to compete in the marketplace?
6. Is the WRC right to argue that the FLA is a tool of industry?
7. If sweatshops are a global problem, what might be a global solution to this problem?

Etch-A-Sketch Ethics

The Ohio Art Company is perhaps best known as the producer of one of the top-selling toys of all time, the venerable Etch-A-Sketch. More than 100 million of the familiar red rectangular drawing toys have been sold since 1960 when it was invented. The late 1990s, however, became a troubled time for the toy's maker. Confronted with

[15] Dara O'Rourke, "Monitoring the Monitors: A Critique of the PricewaterhouseCoopers (PwC) Labor Monitoring," Department of Urban Studies and Planning, MIT.

[16] L. Lee and A. Bernstein, "Who Says Student Protests Don't Matter?" *Business Week*, June 12, 2000, pp. 94–96.

[17] R. Deen, "UW to Join Anti-sweatshop Group," *Seattle Post Intelligencer*, November 20, 2000, p. B2.

[18] "Rights Group Says Nike Isn't Fulfilling Promises," *The Wall Street Journal*, May 16, 2001.

[19] Figures from P. Kenel, "The Sweatshop Dilemma," *Christian Science Monitor*, August 21, 1996, p. 20.

sluggish toy sales, the Ohio Art Company lost money for two years. In December 2000, it made the strategic decision to outsource production of the Etch-A-Sketch toys to Kin Ki Industrial, a leading Chinese toy maker, laying off 100 U.S. workers in the process.

The closure of the Etch-A-Sketch line was not unexpected among employees. The company had already moved the production of other toy lines to China, and most employees knew it was just a matter of time before Etch-A-Sketch went too. Still, the decision was a tough one for the company, which did most of its manufacturing in its home base, the small Ohio town of Bryan (population 8,000). As William Killgallon, the CEO of the Ohio Art Company, noted, the employees who made the product "were like family. It was a necessary financial decision we saw coming for some time, and we did it gradually, product by product. But that doesn't mean it's emotionally easy."

In a small town such as Bryan, the cumulative effect of outsourcing to China has been significant. The tax base is eroding from a loss of manufacturing and a population decline. The local paper is full of notices of home foreclosures and auctions. According to former employees, the biggest hole in their lives after Etch-A-Sketch moved came from the death of a community. For many workers, the company was their family, and now that family was gone.

The rationale for the outsourcing was simple enough. Pressured to keep the cost of Etch-A-Sketch under $10 by big retailers such as Wal-Mart and Toys "R" Us, the Ohio Art Company had to get its costs down or lose money. In this case, unionized workers making $1,500 a month were replaced by Chinese factory workers who made $75 a month. However, according to Killgallon, the main savings came not from lower wages but from lower overhead costs for plant, maintenance, electricity, and payroll, and the ability to get out from the soaring costs of providing health benefits to U.S. manufacturing employees.

The choice of Kin Ki as manufacturer for Etch-A-Sketch was easy—the company had been making pocket-sized Etch-A-Sketch toys for nearly a decade and always delivered on cost. To help Kin Ki, the Ohio Art Company shipped some of its best equipment to the company, and it continues to send crucial raw materials, such as aluminum powder, which is hard to get in China.

The story would have ended there had it not been for an exposé in *The New York Times* in December 2003. The *Times* reporter painted a dismal picture of working conditions at the Kin Ki factory that manufactured the Etch-A-Sketch. According to official Kin Ki publications:

> Workers at Kin Ki make a decent salary, rarely work nights or weekends, and often "hang out along the streets, playing Ping Pong and watching TV." They all have work contracts, pensions, and medical benefits. The factory canteen offers tasty food. The dormitories are comfortable.

Not so, according to Joseph Kahn, the *Times* reporter. He alleged that real-world Kin Ki employees, mostly teenage migrants from internal Chinese provinces, work long hours for 40 percent less than the company claims. They are paid 24 cents per hour, below the legal minimum wage of 33 cents an hour in Shenzhen province where Kin Ki is located. Most do not have pensions, medical benefits, or employment contracts. Production starts at 7:30 a.m. and continues until 10 p.m., with breaks only for lunch and dinner. Saturdays and Sundays are treated as normal workdays. This translates into a work week of seven 12-hour days, or 84 hours a week, well above the standard 40-hour week set by authorities in Shenzhen. Local rules also allow for no more than 32 hours of overtime and stipulate that the employees must be paid 1.5 times the standard hourly wage, but Kin Ki's overtime rate is just 1.3 times base pay.

As for the "comfortable dormitories," the workers sleep head to toe in tiny rooms with windows that are covered with chicken wire. To get into and out of the factories, which are surrounded by high walls, workers must enter and leave through a guarded gate. As for the tasty food, it is apparently a mix of boiled vegetables, beans, and rice, with meat or fish served only twice a month.

The workers at Kin Ki have apparently become restless. They went on strike twice in 2003, demanding higher wages and better working conditions. The company responded by raising wages a few cents and allotting an extra dish of food to each worker per day (but still no more meat)! However, Kin Ki simultaneously made "fried squid" of two workers who were ringleaders of the strike ("fried squid" is apparently a popular term for dismissal). Johnson Tao, a senior executive at the company, denies that the two ringleaders were dismissed for organizing the strikes. Rather, he noted that they were well-known troublemakers who left the factory of their own accord. Mr. Tao acknowledges the low wages at the company, stating, "I know that I need to increase wages to comply with the law. I have the intention of doing this and will raise all wages in 2004."

Meanwhile, in Ohio, William Killgallon, Ohio Art Company's CEO, stated to the *Times* reporter that he considered Kin Ki's executives to be honest and that he had no knowledge of labor problems there. But he said he intended to visit China soon to make sure "they understand what we expect."

Case Discussion Questions

1. Was it ethical of the Ohio Art Company to move production to China? What were the economic *and* social costs and benefits of this decision? What would have happened if production had not been moved?

2. Assuming that the description of working conditions given in *The New York Times* is correct, is it ethical for the Ohio Art Company to continue using Kin Ki to manufacture Etch-A-Sketch toys?
3. Is it possible, as Mr. Killgallon claims, that the Ohio Art Company had no knowledge of labor problems at Kin Ki? Do you think company executives had any knowledge of the working conditions?
4. What steps can executives at the Ohio Art Company take to make sure they do not find the company profiled in *The New York Times* again as an enterprise that benefits from sweatshop labor?

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Western Drug Companies and the AIDS Epidemic in South Africa

In December 1997, the government of South Africa passed a law that authorized two controversial practices. One, called parallel importing, allowed importers in South Africa to purchase drugs from the cheapest source available, regardless of whether the patent holders had given their approval or not. Thus South Africa asserted its right to import "generic versions" of drugs that are still patent protected. The government did this because it claimed to be unable to afford the high cost of medicines that were patent protected. The other practice, called compulsory licensing, permitted the South African government to license local companies to produce cheaper versions of drugs whose patents are held by foreign companies, irrespective of whether the patent holder agreed.

The law seemed to be in violation of international agreements to protect property rights, including a World Trade Organization agreement on patents to which South Africa is a signatory. South Africa, however, insisted that the law was necessary given its own health crisis and the high cost of patented medicines. By 1997, South Africa was wrestling with an AIDS crisis of enormous proportions. It was estimated that over 3 million of the country's 45 million people were infected with the virus at the time, more than in any other country. However, although the AIDS epidemic in South Africa was seen as primary reason for the new law, the law itself was applied to "communicable diseases" (of which AIDS is just one, albeit a devastating one).

Foreign drug manufacturers saw the law as an unbridled attempt to expropriate their intellectual property rights, and 39 foreign companies quickly filed a lawsuit in the country to try to block implementation of the law. Drug manufacturers were particularly concerned about the applicability of the law to all "communicable diseases." They feared that South Africa was the thin end of the wedge, and if the law were allowed to stand, other countries would follow suit. Many Western companies also feared that if poor countries such as South Africa were allowed to buy low-priced generic versions of patent protected drugs, in violation of intellectual property laws, American and European consumers would soon demand the same.

In defense of their patents, the drug companies argued that because drug development is a very expensive, time-consuming, and risky process, they need the protection of intellectual property laws to maintain the incentive to innovate. It can take $800 million and 12 years to develop a drug and bring it to market. Less than one in five compounds that enter clinical trials actually become marketed drugs—the rest fail in trials due to poor efficacy or unfavorable side effects—and of those that make it to market, only 3 of 10 earn profits that exceed their costs of capital. If drug companies could not count on high prices for their few successful products, the drug development process would dry up.

The drug companies have long recognized that countries such as South Africa face special health challenges and lack the money to pay developed world prices. Accordingly, the industry has a history of pricing drugs low or giving them away in the developing world. For example, many AIDS drugs were already being sold to developing nations at large discounts to their prices in the United States. The South African government thought this practice was not good enough. The government was quickly supported by various human rights and AIDS organizations, which cast the case as an attempt by the prosperous multinational drug companies of the West to maintain their intellectual property rights in the face of desperate attempts by an impoverished government to stem a deadly crisis. For their part, the drug companies stated that the case had little to do with AIDS and was really about the right of South Africa to break international law.

While the drug companies may have had international law on their side, the tie-in with the AIDS epidemic clearly put them on the public relations defensive. After a blizzard of negative publicity, and little support from Western governments who were keen not to touch this political "hot potato," several leading manufacturers of AIDS drugs, while still opposing the South African law, started to change their policies. In May 2000, five large manufacturers of AIDS medicines—Merck, Bristol-Myers Squibb, Roche, Glaxo, and Boehringer Ingelhiem—announced that they would negotiate lower priced AIDS drugs in developing countries, primarily in sub-Saharan Africa (some 25 million of the 36 million people infected with the HIV virus in 2000 lived in that region). Still the protests continued.

In February 2001, an Indian drug company, Cipla Ltd, offered to sell a cocktail of 3 AIDS drugs to poor African nations for $600 per patient per year, and for $350 a year to Doctors without Borders (AIDS is commonly treated with a cocktail that combines up to 10 different antiviral drugs). The patents for these drugs were held by Western companies, but Indian law allowed local companies to produce generic versions of patent protected drugs.

The Cipla announcement seemed to galvanize Western drug companies into further action. In March 2001, Merck announced that it would cut the prices of its two AIDS drugs, Crixivan and Stocrin. Crixivan, which sold for $6,016 per year in the United States, would be sold in developing countries for $600 a year. Stocrin, which cost $4,730 a year in the United States, would be sold for $500. Both drugs were often used together as part of an AIDS cocktail. Officials at Doctors without Borders, the Nobel Peace Prize–winning relief agency, welcomed the announcement, but pointed out that in a region where many people lived on less than a dollar a day, the price was still out of reach of many AIDS patients.

A few days later, Bristol-Myers Squibb went further, announcing that it would sell its AIDS drug Zerit to poor nations in Africa for just $0.15 a day, or $54 a patient per year, which was below Zerit's costs of production. In the United States and Europe, Zerit was selling for $3,589 per patient per year. This move was followed by an announcement from Abbott Labs that it would sell two of its AIDS drugs at "no profit" in sub-Saharan Africa.

None of these moves, however, were enough to satisfy critics. In April 2001, the drug companies seemed to come to the conclusion that they were losing the public relations war, and they agreed to drop their suit against the South African government. This opened the way for South Africa to start importing cheap generic versions of patented medicines from producers such as Cipla of India. The decision to drop the suit was widely interpreted in the media as a defeat for the drug companies and a reaffirmation of the ability of the South Africans to enforce compulsory licensing. At the same time, the pharmaceutical companies appear to have gotten assurances from South Africa that locally produced generic versions of patented drugs would only be sold in sub-Saharan Africa and not exported to other regions of the world.

In 2003, Aspen Pharmaceuticals, a South African drug maker, took advantage of the 1997 law to introduce a generic version of Stavudine, and it asked the South African authorities permission to produce up to six more AIDS drugs. Aspen had licensed the rights to produce this drug, and several others, from Bristol-Myers Squibb and Glaxo, the large British company. Bristol and Glaxo had waved their rights to royalties from sales of the drugs in sub-Saharan Africa. At the same time, the companies noted that Aspen was only able to sell the drugs within the sub-Saharan region.

Despite these moves, critics still urged Western drug companies to do more to fight the global AIDS epidemic, which by 2006 was estimated to afflict some 40 million people. For example, in a *New York Times* Op Ed article, noted playwright and AIDS activist Larry Kramer stated that

> It is incumbent upon every manufacturer of every HIV drug to contribute its patents or its drugs free for the salvation of these people. . . . I believe it is evil for drug companies to possess a means of saving lives and then not provide it to the desperate people who need it. What kind of hideous people have we become? It is time to throw out the selfish notion that these companies have the right not to share their patents.

Meanwhile in South Africa, the AIDS epidemic continued on its relentless course. By 2006 it was estimated that one in nine people in South Africa, or 5.5 million people, were infected with HIV, and 800 people a day were dying from AIDS-related complications. In 2003, the South African government had committed itself to offering antiviral drugs at low or no cost to everyone with AIDS. By working with pharmaceutical companies such as Aspen and three Indian producers of generic drugs, the government was able to purchase a cocktail of antiviral HIV drugs for $65 per patient per month. However, by 2006 only 250,000 people were getting antiviral drugs, while at least 700,000 were in urgent need of the drugs. The problem seems to be distribution and particularly a chronic shortage of clinics, doctors, and nurses. Estimates suggested that it may still be years before cheap AIDS drugs are available to all those who need them in South Africa.

Case Discussion Questions

1. Why is it so important for the drug companies to protect their patents?
2. What should the policy of drug companies be toward the pricing of patent-protected drugs for AIDS in poor developing nations such as South Africa?
3. What should the policy be in developed nations? Is it ethical to charge a high price for drugs that treat a life-threatening condition, such as AIDS?
4. In retrospect, could the large Western pharmaceuticals have responded differently to the 1997 South African law? How might they have better taken the initiative?
5. Is AIDS a special case, or should large drug companies make it normal practice to price low or give away patent protected medicines to those who cannot afford them in poor nations?

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Matsushita and Japan's Changing Culture

Established in 1920, the consumer electronics giant Matsushita was at the forefront of the rise of Japan to the status of major economic power during the 1970s and 1980s. Like many other long-standing Japanese businesses, Matsushita was regarded as a bastion of traditional Japanese values based on strong group identification, reciprocal obligations, and loyalty to the company. Several commentators attributed Matsushita's success, and that of the Japanese economy, to the existence of Confucian values in the workplace. At Matsushita, the company took care of employees from "cradle to the grave." Matsushita provided them with a wide range of benefits including cheap housing, guaranteed lifetime employment, seniority-based pay systems, and generous retirement bonuses. In return, Matsushita expected, and got, loyalty and hard work from its employees. To Japan's postwar generation, struggling to recover from the humiliation of defeat, it seemed like a fair bargain. The employees worked hard for the greater good of Matsushita, and Matsushita reciprocated by bestowing "blessings" on employees.

However, culture does not stay constant. According to some observers, the generation born after 1964 lacked the same commitment to traditional Japanese values as their parents. They grew up in a world that was richer, where Western ideas were beginning to make themselves felt, and where the possibilities seemed greater. They did not want to be tied to a company for life, to be a "salaryman." These trends came to the fore in the 1990s, when the Japanese economy entered a prolonged economic slump. As the decade progressed, one Japanese firm after another was forced to change its traditional ways of doing business. Slowly at first, troubled companies started to lay off older workers, effectively abandoning lifetime employment guarantees. As younger people saw this happening, they concluded that loyalty to a company might not be reciprocated, effectively undermining one of the central bargains made in postwar Japan.

Matsushita was one of the last companies to turn its back on Japanese traditions, but in 1998, after years of poor performance, it began to modify traditional practices. The principal agents of change were a group of managers who had extensive experience in Matsushita's overseas operations; they included Kunio Nakamura, who became the chief executive of Matsushita in 2000.

First, Matsushita changed the pay scheme for its 11,000 managers. In the past, the traditional twice-a-year bonuses had been based almost entirely on seniority, but now Matsushita said they would be based on performance. In 1999, Matsushita announced this process would be made transparent; managers would be shown what their performance rankings were and how these fed into pay bonuses. As elementary as this might sound in the West, for Matsushita it represented the beginning of a revolution in human resource practices.

About the same time, Matsushita took aim at the lifetime employment system and the associated perks. Under the new system, recruits were given the choice of three employment options. First, they could sign on to the traditional option. Under this, they were eligible to live in subsidized company housing, go free to company-organized social events, and buy subsidized services such as banking from group companies. They also would receive a retirement bonus equal to two years' salary. Under a second scheme, employees could forgo the guaranteed retirement bonus in exchange for higher starting salaries and keep perks such as cheap company housing. Under a third scheme, they would lose both the retirement bonus and the subsidized services, but they would start at a still higher salary. In its first two years of operation, only 3 percent of recruits chose the third option—suggesting there is still a hankering for the traditional paternalistic relationship—but 41 percent took the second option.

In other ways Matsushita's designs are grander still. As the company has moved into new industries such as software engineering and network communications technology, it has begun to praise democratization of employees, and it has sought to encourage individuality, taking initiative, and risk seeking among its younger employees. In 2002 Matsushita also undertook a significant reorganization, dismantling what had become a Byzantine organizational structure under which performance accountability was difficult to establish, and replacing it with 17 stand-alone worldwide business divisions, each focused on a particular product sector.

However, while such changes may be easy to articulate, they are hard to implement. For all its talk, Matsushita has been slow to dismantle its lifetime employment commitment to those hired under the traditional system. This was underlined in early 2001 when, in response to continued poor performance, Matsushita announced it would close 30 factories in Japan, cut 13,000 jobs, including 1,000 management jobs, and sell a "huge amount of assets" over the next three years. While these actions seemed to indicate a final break with the lifetime employment system—it represented the first layoffs in the company's history—the company also said unneeded management staff would not be fired but would instead be transferred to higher growth areas such as health care.

With so many of its managers products of the old way of doing things, a skeptic might question the ability of the company to turn its intentions into reality. As growth has slowed, Matsushita has had to cut back on its hiring, but its continued commitment to long-standing employees means that the average age of its workforce is rising. In the 1960s it was around 25; by the early 2000s it was 35, a trend that might counteract Matsushita's attempts to revolutionize the workplace, for surely those who benefited from the old system will not give way easily to the new. Still, by 2004 it was clear that Matsushita was making progress. After significant losses in 2002, the company broke even in 2003, started to make profits again in 2004, and in 2005 and 2006 recorded record profits. New growth drivers such as sales of DVD equipment and flat screen TVs certainly helped, but so did the cultural and organizational changes that enabled the company to better exploit these new growth opportunities.

Case Discussion Questions

1. What were the triggers of cultural change in Japan during the 1990s? How is cultural change starting to affect traditional values in Japan?
2. How might Japan's changing culture influence the way Japanese businesses operate in the future? What are the potential implications of such changes for the Japanese economy?
3. How did traditional Japanese culture benefit Matsushita during the period from the 1950s to the 1980s? Did traditional values become more of a liability during the 1990s and early 2000s? How so?
4. What is Matsushita trying to achieve with human resource changes it has announced? What are the impediments to successfully implementing these changes? What are the implications for Matsushita if (*a*) the changes are made quickly or (*b*) it takes years or even decades to fully implement the changes?
5. Why do you think Matsushita reorganized itself into stand-alone worldwide business divisions?
6. What does the Matsushita case teach you about the relationship between societal culture and business success?

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Mired in Corruption—Kellogg, Brown & Root in Nigeria

In 1998 the large Texas-based oil and gas service firm, Halliburton, acquired Dresser Industries. Among other businesses, Dresser owned M. W. Kellogg, one of the world's largest general contractors for construction projects in distant parts of the globe. After the acquisition, Kellogg was combined with an existing Halliburton business and renamed Kellogg Brown & Root, or KBR for short. At the time it looked like a good deal for Halliburton. Among other things, Kellogg was involved in a four-firm consortium that was building a series of liquefied natural gas (LNG) plants in Nigeria. By early 2004, the total value of the contracts associated with these plants had exceeded $8 billion.

In early 2005, however, Halliburton put KBR up for sale. The sale was seen as an attempt by Halliburton to distance itself from several scandals that had engulfed KBR. One of these concerned allegations that KBR had systematically overcharged the Pentagon for services it provided to the U.S. military in Iraq. Another scandal, centered on the Nigerian LNG plants, involved KBR employees, several former officials of the Nigerian government, and a mysterious British lawyer called Jeffrey Tesler.

The roots of the Nigerian scandal date back to 1994 when Kellogg and its consortium partners were trying to win an initial contract from the Nigerian government to build two LNG plants. The contract was valued at around $2 billion. Each of the four firms held a 25 percent stake in the consortium, and each had veto power over its decisions. Kellogg employees held many of the top positions at the consortium, and two of the other members, Technip of France and JGC of Japan, have claimed that Kellogg managed the consortium (the fourth member, ENI of Italy, has not made any statement regarding management).

The KBR consortium was one of two to submit a bid on the initial contract, and its bid was the lower of the two. By early 1995 the KBR consortium was deep in final negotiations on the contract. It was at this point that Nigeria's oil minister had a falling out with the country's military dictator, General Abacha, and was replaced by Dan Etete. Mr. Etete proved to be far less accommodating to the KBR consortium, and suddenly the entire deal looked to be in jeopardy. According to some observers, Dan Etete was a tough customer who immediately began to use his influence over the LNG project for personal gain. Whether this is true or not, what is known is that the KBR consortium quickly entered into a contract with the British lawyer, Jeffrey Tesler. The contract, signed by a Kellogg executive, called on Tesler to obtain government permits for the LNG project, maintain good relations with government officials, and provide advice on sales strategy. Tesler's fee for these services was $60 million.

Tesler, it turned out, had long-standing relations with some 20 to 30 senior Nigerian government and military officials. In his capacity as a lawyer, he had handled their London affairs for years, helping the Nigerian officials purchase real estate and set up financial accounts. Kellogg had a relationship with Tesler that dated back to the mid-1980s, when they had employed him to broker the sale of Kellogg's minority interest in a Nigerian fertilizer plant to the Nigerian government.

What happened next is currently the subject of government investigations in France, Nigeria, and the United States. The suspicion is that Tesler promised to funnel big sums to Nigerian government officials if the deal was done. Investigators base these suspicions on a number of factors, including the known corruption of General Abacha's government, the size of the payment to Tesler, which seemed out of proportion to the services he was contracted to provide, and a series of notes turned up by internal investigators at Halliburton. The handwritten notes, taken by Wojciech Chodan, a Kellogg executive, document a meeting between Chodan and Tesler in which they discussed the possibility of channeling $40 million of Tesler's $60 million payment to General Abacha.

It is not known whether a bribe was actually paid. What is known is that in December 1995, Nigeria awarded the $2 billion contract to the KBR consortium. The LNG plant soon became a success. Nigeria contracted to build a second plant in 1999, two more in 2002, and a sixth in July 2004. KBR rehired Jeffrey Tesler in 1999 and again in 2001 to help secure the new contracts, all of which it won. In total, the KBR consortium paid Tesler some $132.3 million from 1994 to early 2004.

Tesler's involvement in the project might have remained unknown were it not for an unrelated event. Georges Krammer, an employee of the French company Technip, which along with KBR was a member of the consortium, was charged by the French government for embezzlement. When Technip refused to defend Krammer, he turned around and aired what he perceived to be Technip's dirty linen. This included the payments to Tesler to secure the Nigeria LNG contracts.

This turn of events led French and Swiss officials to investigate Tesler's Swiss bank accounts. They discovered that Tesler was kicking back some of the funds he received to executives in the consortium and at subcontractors. One of the alleged kickbacks was a transfer of $5 million from Tesler's account to that of Albert J. "Jack" Stanley, who had been head of M. W. Kellogg and then Halliburton's KBR unit. Tesler also transferred some $2.5 million into Swiss bank accounts held under a false name by the Nigerian oil minister, Dan Etete.

Other payments included a $1 million transfer into an account controlled by Wojciech Chodan, the former Kellogg executive whose extensive handwritten notes suggest the payment of a bribe to General Abacha, and $5 million to a German subcontractor on the LNG project in exchange for "information and advice."

After this all came out in June 2004, Halliburton promptly fired Jack Stanley and severed its long-standing relationship with Jeffrey Tesler, asking its three partners in the Nigeria consortium to do the same. The United States Justice Department took things further, establishing a grand jury investigation to determine if Halliburton, through its KBR subsidiary, had been in violation of the Foreign Corrupt Practices Act. In November 2004 the Justice Department widened its investigation to include payments in connection with the Nigeria fertilizer plant that Kellogg had been involved with during the 1980s under the leadership of Jack Stanley. In March 2005, the Justice Department also stated that it was looking at whether Jack Stanley had tried to coordinate bidding with rivals and fix prices on certain foreign construction projects. As of mid-2007, the U.S. investigation was still ongoing.

Case Discussion Questions

1. Could Jeffrey Tesler's alleged payment of bribes to Nigerian government officials be considered "facilitating payments" or "speed money" under the terms of the Foreign Corrupt Practices Act?
2. Irrespective of the legality of any payments that Tesler may have made, do you think it was reasonable for KBR to hire him as an intermediary?
3. Given the known corruption of the Abacha government in Nigeria, should Kellogg and its successor, KBR, have had a policy in place to deal with bribery and corruption? What might that policy have looked like?
4. Should KBR have walked away from the Nigerian LNG project once it became clear that the payment of bribes might be required to secure the contract?
5. There is evidence that Jack Stanley, the former head of M.W. Kellogg and KBR, may have taken kickback payments from Tesler. At least one other former Kellogg employee, Wojciech Chodan, may have taken kickback payments. What does this tell you about the possible nature of the ethical climate at Kellogg and then KBR?
6. Should Halliburton be called to account if it is shown that its KBR unit used bribery to gain business in Nigeria? To what extent should a corporation and its officers be held accountable for ethically suspect activities by the managers in one of its subsidiaries, particularly given that many of those activities were initiated before Halliburton owned the subsidiary?

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