

## **Imperfect Markets: Business Ethics as an Easy Virtue**

ABSTRACT. This paper marks a radical diversion from the large body of prevailing literature in business ethics which primarily views the issue in individual-personal terms, i.e. corporate executive and the employee, and suggests that making corporations more ethical would probably come through changes in executive behavior. While this approach has strong intellectual roots in moral philosophy and religion, it fails in explaining the persistence of unethical and illegal behavior among corporations of all sizes, financial health, competitive market conditions, and, level of individual executive compensation. This paper argues for a fundamentally different approach to understanding ethical behavior, or lack thereof, among corporations and their executives. It is asserted that an overwhelmingly large rationale and/or inducement for proactive ethical business behavior is rooted in competitive aspects of particular markets, and industry structures prevailing in those markets. Furthermore, while highly competitive markets may promote efficiency, they do not guarantee ethical behavior and may indeed provide greater opportunities and incentives for unethical business behavior. Thus, by following the current prognosis, we could be wasting enormous resources in terms of teaching business ethics, and creating and imposing corporate codes of conduct. We assert that these approaches would at best make a marginal improvement in the ethical performance of corporations while at the same time exacerbate the problem by ignoring more fundamental, structural issues. Imperfect markets, with their above-market profits, are a necessary but insufficient condition for corporations to behave ethically. It is only under imperfect markets that individual executives can play an important role in guiding their corporations toward great ethical norms. These are undertaken for a variety of reasons, including, protecting a corporations

good name, public expectations, competitive norms, and, corporate culture and individual executive's predilections, to name a few.

The institutional context of business ethics has become an increasing concern for enquiry among management scholar, other social scientists, corporate executives and political leaders. To wit, what are the conditions, i.e., external sociopolitical and competitive structures, and intra-institutional frameworks, that propel and instigate corporations and their executives to indulge in unethical and even illegal actions that they would otherwise condemn when undertaken by others. The point is not merely rhetorical, it raises important issues of public policy and social organization. At the micro level, it is the individual conduct acting in a business context that gets reflected in the adverse social impact of the business institution. Philosophers and ethicists have almost invariably referred to this aspect of business behavior contending that moral values find their expression only through human beings acting either individually or collectively. The macro or the structural context of business ethics is even more important. As economic activity increases in complexity and technological orientation, it is unhinged from the mooring of individual actions. Large scale economic activity, ironically, calls for collective action where each individual contributes but a tiny fraction to the whole and where individual acts are rewarded and punished not so much for their ethical content, but on the notion of one's loyalty to the institution where individual morality and institutional welfare, however defined, are perceived to be in conflict.

The paramount question for us to examine involves the circumstances, individual and contextual, that make business people and business institutions act in socially harmful ways. We must ask whether there are levels of unethical activity and immoral behavior that

would persist under different types of economic conditions and individual proclivities regardless of a society's efforts to curb such behavior and which, therefore, must be accepted as the necessary cost of doing business. Market systems with their self-correcting discipline and competitive forces, however, are presumed to keep such behavior at a minimum compared to alternatives for organizing economic activity, i.e., state control of production and distribution systems. Therefore, among a constellation of imperfect worlds, a market economy with individuals exercising their free will to make choices, is said to offer the least repugnant of alternatives and the one with the greatest susceptibility toward responding to corrective mechanisms. It is this proposition which is the subject of our enquiry and to which we now turn our attention.

### **Business ethics in a historical context**

Concern about business ethics, or lack thereof, seems to be a historical phenomenon which appears with remarkable regularity through periods of economic prosperity and hard times. One can easily recall significant periods in American history, and for that matter in the history of most capitalistic nations, when major business scandals assaulted the nation's moral psyche and its denizens' pocketbooks. Witness the price-rigging conspiracy among such electrical industry giants as GE and Westinghouse in the 1950s which led to a flurry of lawsuits, swindled the nation's economy in an enormous way and sent many senior corporate executives to jail (Cook, 1966; Fuller, 1962; Herling, 1962). The Electrical Conspiracy is not an isolated historical example of ethical drama unfolding within the walls of corporate America. Scandals like The Tea Pot Dome and robber barons of yesteryear have easily been relegated to the status of anachronisms by the sheer audacity, greed and a callous disregard for society's standards of their latter-day

peers. The eighties will be remembered in the United States as much for “Reaganomics” and “get-the-government-off people’s backs”, as for the decade of greed personified by such luminaries as Ivan Boesky, Mike Milken and Charles Keating, to name a few (Binstein and Bowden, 1993; Burrough and Helyar, 1990; Day, 1993; Lewis 1989; Lorsch, 1989; Stewart, 1991; Vise and Coll, 1991).

We are never tired of being told that a majority of business institutions and executives are honest, ethical and law abiding. It is only the deviant few from whom the business system and society needs to be protected. This statement, however, begs to the question rather than answers it. Majorities are always honest, caring and suffused with intrinsic humanistic values. They are also largely law-abiding and operate according to society’s standards of acceptable behavior whether driven by an innate sense of good conduct for fear of social reprobation. Otherwise social organizations could not survive and civilized society’s standards of acceptable behavior whether driven by an innate sense of good conduct or fear of social reprobation. Otherwise social organizations could not survive and civilized societies would cease to exist.

### **Lack of business ethics – it’s the adversity, stupid!**

Ethical lapses and illegal behavior are not the domain of some sleazy firms operating at the fringes of otherwise respectable and responsible companies. On the contrary, they are to be found in every segment of business activity, afflicting corporations large and small, and regardless of their financial and market circumstances. While a large majority of all business operates within the socially and legally acceptable standards of corporate behavior, the deviant corporations and executives do not necessarily display structural, institutional, or even personal characteristics that are different from their more

ethical counterparts. In many cases, it is the same corporation that receives public accolades for exemplary behavior in one aspect of its business while at the same time being hauled into the court of public opinion and the judicial arena for acts of moral reprobation and illegal behavior.

We have insider trading, money laundering, brokerage account churning and saving and loan scandals in the banking and finance industry. The willful violence against our environment can be traced to major firms in chemical, forestry and other heavy industries. Food companies are not averse to selling adulterated foods and resort to bid rigging and price fixing in feeding programs for the poor. Pricing for what the market will bear – regardless of how it might affect the most vulnerable amongst us – is not confined to the pharmaceutical industry. Even companies engaged in the national defense effort are not averse to using unethical means to secure business. Bidding for inside information, cost inflation through account padding, inadequate product testing and shoddy manufacturing practices are all part of a day's work and are not confined to a deviant few, but have been found to be widely practiced behaviors (Holcomb and Sethi, 1992; Sethi, 1981). In marketing abroad, multinational corporations (MNCs) are equally indiscriminate in selling products, e.g., infant formula, cigarettes, chemicals and pesticides, prescription and over-the-counter drugs, in a manner that would be considered unethical and illegal at home, with nary a word of caution or disclosure, to a set of customers who are even less equipped to make informed choices. In their overseas operations, MNC's search for ever lower costs, and, in the process, they become deliberately ignorant, or at best indifferent, to the hazardous working conditions, starvation level wages, and environmental degradation that inflict many Third World countries as these countries constantly compete

with each other for the privilege of serving the economically powerful multinational behemoths (Donaldson, 1989; Guyon 1992; Sethi and Steidlmeier, 1991; Shrivastava, 1987).

### **Perfect competition and business ethics**

Competition keeps businesses honest. It should, therefore follow that firms would act more ethically, even in the economic sense of maximizing social welfare, as markets approximate the ideal conditions of perfect competition. Competitive markets strive for productivity and allocative efficiency and thereby serve the general welfare even when the business person is pursuing his/her own self-interest and is not concerned about promoting general welfare. Unfortunately, this is not the case when applied to business morality. While efficient markets may prompt firms to act smart, they do not induce them to act ethically, and, “‘perfect’ markets are highly imperfect in their enforcement of business morality” (Baumol, 1991, p.24). Indeed, a counter-intuitive argument could be made to suggest that perfect competition creates the conditions that are ripe for unethical behavior.

Briefly described, the conditions of ideal markets include the existence of a large number of buyers and sellers none of whom is able to influence the total supply or demand; the objects of exchange are completely divisible into exchangeable units, and the parties who are not subject to the transaction can be excluded from the benefits of the exchange; there are no externalities, i.e., spill-over benefits or costs going to non-exchange parties; and, exchange transactions incur no costs and there are no entry barriers (Harris and Carman, 1991).

The absolute discipline of ideal markets leaves little room for the individual firm to undertake voluntary activities that go beyond what is legally required and which all other

parties are obligated to perform. To do so otherwise would incur additional costs that a firm could not absorb since buyers, being perfectly informed, would refuse to pay higher prices for products that could be bought more cheaply elsewhere. The requirements of perfect competition, and its concomitant condition of a large number of miniscule and homogeneous firms with no individual distinguishing features with which the consumers may identify, are by themselves

enough to undermine the working of market mechanism... An anonymous supplier who looks like every other supplier to potential customers will risk little or no loss of reputation by product degradation... These are precisely the conditions that lead to repeated games of market reality to be populated by transient players... because of the implied or explicit assumption that sunk costs are absent, firms lose nothing by entering a market, milking any profits it has to offer to those prepared to use fair means or foul, and then exiting it in haste if and when past misconduct makes their continuing presence uncomfortable (Baumol, 1991, p.9).

One of the most notable exceptions to this behavior pattern should occur when firms are deemed to gain competitive advantage by hiring members of minority groups at lower wages because they are being discriminated against by other companies. Thus it would seem that competitive markets should induce more ethical non-discriminatory behavior in the market place. However, in practice this does not happen even where such discrimination is widely applied. In such cases, society enforces discriminating behavior uniformly, through a web of social coercions, both legal and extra legal, which prevent individual firms from exercising free choice under the threat of communal boycott of its products and services and social ostracism of offending firms. We have only to look in our own backyards to realize the potency of collective exploitation on the part of those who

possess power against those who do not. The cases in point range all over the world from the Blacks of South Africa, the untouchables of India, native pre-colonial populations in scores of Latin American countries, and minorities of all ilk and persuasions in the United States, Europe, Japan, Far East and the Middle East.

### **Lack of business ethics – the devil made me do it!**

A related explanation for unethical business practices can be found in the “deviant executive” syndrome. This explanation, however, is grossly inadequate given the systematic pattern of illegal and unethical behavior that persists in all industrial and corporate sectors and where the executives involved – like their companies – exhibit no differences in their socio-economic and other discernible characteristics. Business people are no more immune to illicit temptations and unethical behavior than other mortals. They are also equally capable of acts of high moral courage and personal integrity. An executive’s financial circumstances also do not appear to be related to his/her unethical behavior. Nor is it a particular trait of the entrepreneurial empire builder as against the corporate mogul in the pin-stripe suit. Money has no conscience and no memory. Some of the most egregious white-collar crimes of the eighties were committed by executives who would be comfortable in every type of business situation and whose financial wealth would be the envy of most earthlings.

An alternative, and more logical, proposition might be found in the argument that these executives are driven by rational calculations in enhancing their personal and corporate wealth where the opportunity for gain far exceeds the risk of being caught and punished. Even in the event of being apprehended, the legal guilt rarely gets transferred

into social ostracism. Propelled by their competitive urges to do one better than one's peers, ethical and moral concerns get pushed lower on one's value hierarchy. Acts of executive unethical behavior are not confined to a company's external constituencies. They also manifest themselves in dealing with a company's legal owners, i.e. stockholders. Through their control of corporate boards, executives successfully manage to increase their incomes while delivering less than stellar performance to the stockholders, consistently keeping them in the dark as to the size and scope of their compensation beyond legally mandated disclosure requirements (Roberts, 1992; Sethi and Namiki, 1987).

Corporate decision-making processes also mitigate against individual employees or managers to pursue ethical standards similar to those they would apply in their personal conduct outside the corporate context. Group norms, and pressure to conform, exert strong influence on individuals to yield to demands for lower ethical standards when they are seen to be protecting the group at the cost of potential harm to "outsiders". Corporate decisions, from conception to implementation, involve hundreds and often thousands of individuals, each contributing an infinitesimal amount, and often with little or no understanding and appreciation as to its potential impact on the overall decision. Thus divorced from the consequences of collective outcome, the employee focuses on the cost/benefit analysis of his/her decision primarily in personal terms where the collective harm of an anti-social choice is rarely apparent. We become hostage to the tyranny of small decisions. The group orientation of corporate unethical behavior depersonalizes business leadership. Thus, while the impact of an unethical or anti-social act may be more serious for the society when compared with a multiplicity of personal unethical acts

committed by individuals in their private capacity, the corporate personality diffuses the individual burden of guilt.

### **Imperfect markets: opportunities for being virtuous**

From the foregoing discussion, we must conclude that prevailing conventional explanations of why corporations and managers behave unethically, and how they might be induced to do otherwise, are inconsistent with available evidence. Instead, we must look for those structural, institutional, and individual attributes that explain ethical business behavior under normal operating conditions, and relate to the overwhelming majority of business actions in the marketplace.

There are two conditions – given the competitive nature of markets – that must exist in order to create a potentially conducive environment for business to behave ethically: (1) there must be some imperfections in the marketplace that the firm can exploit to generate “above normal” profits., i.e., strategic slack; (2) the firm must be assured of garnering both economic and non-economic benefits from such ethical conduct in terms of greater customer loyalty, public goodwill and trust, employee satisfaction, and, reduced government regulation and oversight, to name a few. A part of these profits could then be used by the firm to go beyond what is minimally or legally required to sustain one’s competitive position.

Existence of strategic slack is a necessary but not a sufficient condition for companies to act more ethically than their competitors in the marketplace. Although it provides the resources to enhance managerial discretion, it does not direct it. A company’s management may use its “slack” resources to enhance its ethical posture. It could just as

easily use them to defy societal expectations and resist external strategies (Falbe and Sethi, 1989). For example, even a cursory examination of business practices prevailing in large market segments all over the world would suggest that under conditions of oligopoly and market concentration firms invariably resort to non-price competition, suppressing information that would allow customers to make informed choices and providing only that information which would lead customers would find difficult to evaluate, thereby allowing the firm to charge premium prices for little or no added value.

The second necessary condition, i.e., market reward for firm's enhanced ethical and socially desirable behavior, is also rooted in market imperfections especially as they relate to market concentration. Contrary to the conditions of ideal markets, the long-term prosperity and growth of company depends on its ability to make those very conditions inoperable, i.e., the firm must: become known to the customer; seek customers' loyalty and repeat business through offering them quality products, adequate information as to their appropriate use, and at competitive prices; deal with its stockholders, employees and suppliers in a fair and equitable manner to ensure their continuous support and inflow of resource inputs; treat the community-at-large fairly so as to maintain a high level of socio-political trust; and, nurture a corporate culture that puts high value on ethical and socially responsible behavior as an integral part of doing business and corporate ethos (Baumol, 1991; Heal, 1976; Sethi, 1994). A reputable firm inspires trust and confidence. This reduces the customers' cost of learning as they accept the company's claims and assurances as to product quality and service and thereby reduce the latter's transaction costs. Thus it behooves the firm to sacrifice at least some of its short-term profits arising

out of market imperfections and use them to build greater entry barriers against its competitors and thereby insure long-term, above-normal profitability for the enterprise.

Notwithstanding, a firm does not have to use its strategic slack in an ethically proactive and socially responsible manner. Market conditions may induce the firm to maximize short-term profits because it does not see long-term advantage in such a trade-off. The ideological orientation of management may influence its behavior by disregarding the needs of the general community and those stakeholders who cannot directly impact its operations. On a more personal level, top managers may also choose to use strategic slack-based discretion in philanthropic and other activities that give them personal pleasure and a sense of power although these activities might be inappropriate or have low priority for the community-at-large. Thus, “management uniqueness: or the sum total of all those factors that define the corporate personality, plays an important part in the use of strategic slack in influencing a company’s ethical posture (Baumol, 1991; Sethi, 1994; Sethi and Steidlmeier, 1991). Strategic slack affords management the arrogance of power to respond negatively to external forces of change. A self-assured and self-righteous management may be willing to tolerate a high degree of mis-match between corporate behavior and external environmental expectations thereby causing a higher level and an extended period of dissonance between the corporation and its adversaries (Nystrom and Starbuck, 1984; Pettigrew, 1973; Sethi, 1994). Alternately, strategic slack may provide corporate management with an opportunity to experiment, fashion innovative solutions, and respond proactively to external forces of change. A self-assured and yet tolerant management, when cushioned with a high level of current profits, may be willing to take a

longer term perspective of the situation and move more rapidly to reduce the level of mismatch in adapting to changes in its external environment.

### **Imperfect markets and impediments to being virtuous**

A large part of business activity in most industrialized countries is accounted for by industries that are obligopolistic in character. Moreover, as new technologies grow and mature, and new markets are discovered and nurtured, they invariably acquire the characteristics of obligopolistic structures. Imperfect markets have become a dominant condition of capitalistic societies and are likely to remain so for the foreseeable future. It is also not clear whether perfect competition, or conditions approaching it, is indeed feasible or desirable for the efficient working of large and complex industrialized market economies.

This raises an important question. To wit, under a persistent condition of imperfect markets, how can the large corporation be induced to act ethically and socially-proactively, without the burden of onerous governmental regulation and oversight, and thereby minimize the cost of regulatory failure?

At one rational level, industries and companies should strive to act ethically so as to maintain the viability and social acquiescence of imperfect markets and preserve their franchises. There is enough rhetoric and some action to suggest that business recognizes the essentiality of this argument. In practice, however, this condition is more often violated even when it is apparent that observance of higher ethical standards would best serve not only the community's interest but also that of the businesses involved. There are two possible explanations for this anomalous behavior. The first one has to do with the character of public and private goods in society and the social means of distributing public

goods, and social criteria of converting public goods into private goods. The second one pertains to the nature of the intellectual core and value set of the business institution, industry structure, and, value orientation and reward framework of top corporate managers.

The endemic character of business-society conflicts in market economies and democratic societies has to do with the nature of public-collective goods and private goods. The former are viewed as society's endowments to be shared by all of its members without regard to one's ability to pay for them. The distributive criteria are those of need social relevance and collective enjoyment. Private goods are for the exclusive enjoyment of their owners and, within broad limits, to be bought, sold and exchanged at their owners' discretion. In general, market institutions are not equipped to deliver collective goods and may fail completely at the collective provision of social norms. Expansion of market activities, by its very nature, creates more private goods, often contracting the supply of public goods. While business institutions are applauded for their production of private goods and services, they also take the major blame for depleting the stock of public goods.

In one sense, society's moral and ethical values are public goods. All members of a society stand to benefit from an enhancement of these values regardless of their individual contribution to such enhancement. Here the nature of corporate mission and goals and those of private voluntary organizations (PVOs) stand in sharp contrast. It may partially explain the inherent discrepancy in public trust and goodwill enjoyed by public interest groups against that of the business community (Granovetter, 1985; Hirsch, 1976; McNutt, 1988; Sen, 1973, 1985, 1987; Yaari, 1981). The *intellectual core* and *value set* of the

corporate entity are rooted in the premise that individuals and groups have the right to produce and exchange good and services which the society needs and at prices which are competitively determined in the marketplace. The success of a corporation is determined in direct proportion to its ability to serve public needs. Profits are one measure of a corporation's reward for doing its job well. In the strict sense of the word, the most profitable corporation is also the most socially responsible corporation because it has satisfied the needs of a large segment of society.

Unfortunately, this state of affairs creates real problems for those firms that wish to act ethically and thereby increase the common stock of society's moral values. In the case of other social institutions, i.e., PVOs, e.g., churches, universities and charitable institutions, there is a presumption of altruism which is further strengthened by their espoused mission and goals. Even where one of these institutions acts in a manner which could be construed to be antisocial in some quarters, it is still viewed as only acting for some larger social good. The problems of the free rider, i.e., one who takes a greater share of public-collective goods without adequately contributing to the enhancement of their stock or being concerned about depriving others of similar enjoyment, are not applicable. PVOs are expected to behave in the public interest. It is their *raison d'être*. Ergo, there is no free rider (Sethi, 1994).

Private firms face exactly the opposite problem. They must always try to maximize private gains by internalizing all possible profits and externalizing all possible costs. Even under conditions of imperfect markets, dominant firms cannot always control – for legal and other reasons – the behavior of rogue firms wishing to exploit an industry's stock of public trust for their own gain, i.e., become a free rider. This condition is likely to

exacerbate where public trust in an industry or a firm's integrity is quite high; the offending firm stands to garner significant financial reward for being a free rider; and especially where retaliation by the industry or society is likely to be too late or too little and would cause the offending firm proportionately less harm because of its smaller market stake.

Industry members, therefore, must assume that other companies would follow suit and behave equally aggressively as free riders since they have more to lose from contributing to general public trust and moral and ethical values and everything to gain from being a free rider. Conversely, while dominant firms stand to lose through the actions of the free rider, they also stand to gain by acting in concert and maintaining industry cohesiveness which provides some restraints to constantly lowering standards by industry members. On the other hand, where industry standards of ethical norms are low, and so perceived by the public-at-large, a deviance by an industry member to raise ethical standards and undermine industry's public stance would be severely resisted by the rest of the industry with the deviant member subjected to intense public and private pressure to fall in line.

The one exception to this rule would take place where a firm's market position and resultant non-market rent are so strong that it must protect them at all costs by courting the goodwill of its customers, government regulators and public-at-large (Hirsch, 1976; Schelling, 1971, 1978). The incentive to do so, however, is not altruism but a desire to preserve the firm's extra profits. The benefit of public goodwill is measured in terms of potential profits. This condition tends to undermine the value of a firm's contributions to enhancing society's stock of ethical and moral values because companies are viewed to be primarily acting in self-interest thereby discounting their claims of being disinterested

public citizens. Even when corporations engage in philanthropic activities that are not designed solely to ameliorate the second-order effects of their normal business activities, they dilute their social import and the altruistic character of their “public or collective goods” by linking them to those groups and activities that further a corporation’s commercial goals by labeling them “strategic giving”.

A third problem pertaining to companies’ reluctance to pursue higher ethical standards is related to the authority and power of top managers within a company’s organization structure: the nature of their rewards, financial and non-financial, private and social; the reference group to which these managers aspire to belong; and, how these managers view themselves and are in turn viewed by society. Received legal theory and corporate hyperbole suggest that a company’s managers work primarily to enhance the best interests of the firm’s owners, i.e., stockholders, commensurate with some measure of acceptable risk. Where interests of other stakeholders, e.g., employees, customers, are considered, they are balanced within the framework of a corporation’s long term survival and growth and not in terms of their inherent benefit to these stakeholders. However, in practice this is far from true. While corporate managers may perpetuate such a myth in order to protect their authority and power, there is ample evidence to suggest that managers do not always act in the best interest of stockholders. The rapid turnover in stockholders, and the increasingly institutional character of stockholdings, make stockholder governance less than effective. Top managers hold most of the cards in controlling the destiny of the corporation and, except in dire circumstances, are hard to replace by discontented stockholders. Furthermore, this situation is unlikely to change in the foreseeable future despite some recent, widely publicized examples of boardroom

revolt resulting in the ouster of CEOs in companies like American Express, General Motors, IBM and Sears, Roebuck (Bolton, 1993; Dobrzynski, 1993; Loomis, 1993; Magnet, 1992, 1993; Monks and Minow, 1991; Pulliam, 1993; Pulliam and Patterson, 1993; Rowe, 1993; Saporito, 1993; Stewart, 1993). In the absence of fundamental changes in incorporation laws, SEC oversight, management control of board election processes, and shareholder activism, these examples would remain what they are, i.e., aberrations that show the magnitude of the problem rather than avenues of solution. Studies also suggest that there is little correlation between top management compensation and corporate performance either in the short or in the long run (Byrne, 1993; Crystal, 1992; Drucker, 1984; Leonard, 1990; Longnecker et al., 1992; Murphy, 1985; Redling, 1981; Sethi and Namiki, 1987; Wilson et al., 1992).

The self-interest orientation of the corporation; the arbitrary character and self-perpetuating nature of managerial authority; and, public perception of top management's pursuit of self-interest at the expense of a company's legitimate owners, other significant stakeholders, and society-at-large; all combine to create an aura of low public legitimacy and esteem for corporate managers, especially those of large, publicly-held enterprises. Devoid of public accolades and respect given almost automatically to the leaders of most other major social institutions, corporate managers turn to their own peer group, i.e., other business leaders, for legitimization of their behavior, perquisites, and social *raison d'être*. Thus individual corporate ethical standards mimic closely those of the industry, business in general, and the reference group of a company's top managers, i.e., top managers of other companies.

Top managers as a group, therefore, seek legitimacy of their authority and power in reference to those objects and activities that command high value and prestige within their reference group. These include, among others: the absolute size of the corporation, assets and resources that they control; their financial compensation and perquisites of office; board membership of other large corporations; and, trusteeships and board positions among a select group of highly prestigious cultural, educational, and philanthropic organizations, that lend further credence to their sense of self-esteem within a particular reference group. Since cries of lowered ethical standards and a declining sense of social responsibility are invariably made by individuals and groups outside their milieu and are considered hostile to private enterprise, these views are tolerated by the corporate managers only to the minimum extent necessary. Similarly, political/legislative initiatives to improve corporate morality are viewed with disdain since they are seen to be originating from politicians whose own moral standards are even more suspect and whose initiatives can be modified through pro-business advocacy and other means of political representation.

### **Making ethical behavior and attractive option for managers and corporations**

It would seem almost counter-intuitive to suggest that economic institutions could ever be made to seek altruistic goals as an end in themselves, or at least, as an integral part of their overall objectives. And yet, this is precisely what needs to be done if we are to achieve an ascension in the ethical norms of corporate institutional behavior. We also contend that the ethical behavior of individual managers and employees, acting either in their personal or institutional capacities, but within the corporate institutional framework,

would similarly be improved to a great extent by the existence of supportive institutional and social incentives rather than merely proscriptive exhortations or punishments. While exemplary and extraordinary altruistic individual behavior might give us our heroes, they would certainly not be the heroes that ordinary mortals could emulate in the routines of their everyday lives. Nor do these heroes, and villains, provide us with an adequate basis for structural analysis of social institutions. The emphasis in our effort, therefore, must be on those social-structural underpinnings and institutional frameworks that are necessary for improving the ethical norms of corporate behavior.

American society, hitherto, has largely resorted to the use of the use of legally imposed proscriptive measures where the focus of regulatory behavior is on controlling negative deviation from a base level of social norms of ethical conduct leaving positive deviation largely to the discretion and individual proclivities of corporations and managers involved. It is also apparent that legal approaches to inducing more ethically responsive corporate behavior, while necessary, will at best provide a minimal level of commonly accepted standard – a standard which the organized business groups constantly attempt to erode and evade. The critical need, therefore, is to create a proper balance between regulatory proscriptions and means of social persuasion for proactive ethical behavior. Our challenge is to seek ways and means by which economic institutions and their leaders are induced to act in a more ethical and socially proactive manner and with minimal resort to mandated governmental controls and their concomitant cost of policing and enforcement.

## **Social means for enhancing proactive corporate ethical behavior**

The intensity of prevailing ethical norms in a society provides a good framework to create social carrots for inducing enhanced ethical standards of institutional behavior. To act ethically is less onerous in a social environment where mutual interdependence is strong and where social acquiescence is necessary for the realization of individual goals. It is not surprising, therefore, that variance from group norms is minimal under conditions of cultural homogeneity, shared values and group orientation in social organization. Thus ethical standards of behavior can be collectively raised without incurring excessive costs of policing and regulation on the one hand and leakages from the free rider problem on the other hand.

The role of a company's top managers is extremely important in influencing a corporation's norms of ethical conduct within the parameters outlined in the earlier part of this paper. While public exposure of the damage to society as a whole will help promote a social ethos, it will not be sufficient to secure it so long as individualistic behavior retains its legitimacy over large areas of collective action (Hirsch, 1976). According to Erich Fromm (1949),

It is the function of the social character to shape the energies of the members in such a way that their behavior is not left to conscious decisions whether or not to follow the social pattern but that people want to act and at the same time find gratification in acting according to the requirements of the culture. In other words, the social character has the function of molding human energy for the purpose of the functioning of a given society.

Nowhere is this concept more relevant than in the role and actions of corporate chief executive officers (CEOs) and other top managers. Studies show that most corporate CEOs are appointed from within their own companies, consider their first loyalty to their firms, and tend to have fewer interests outside the affairs of the companies they manage and CEOs of other companies with whom they interact. Corporate managers, like most professionals, seek peer group approval. Unfortunately, their peer group is extremely narrowly based and consists primarily of other CEOs or senior corporate managers. This narrow peer group seeks and measures “power and prestige...very largely in direct proportion to status in the corporate community acquired during a career. Conspicuous consumption and overt signs of wealth are used as class symbols in the fashion of Veblen’s ‘leisure class’” (Sethi et al. 1984, pp. 119-120). Conversely, a significant deviation from the prevailing norms of acceptable within group conduct exposes the CEO to peer group contempt, injures his/her self-esteem, and risks his/her financial well-being by curtailing job mobility and other opportunities for income generation and wealth enhancement.

### **Altruism as a desirable institutional and personal goal**

An important characteristic of the American socio-political system, unlike many other societies, is that most corporate leaders do not come from established social elites. Nor do they have recognized symbols of social class such as titles. Moreover, they are grossly under-represented in peak social institutions of status or considered social elites and positive role models, e.g., scientists and educators, representing society’s higher moral and aesthetic values. The public-at-large has little familiarity with their individual

personalities and character, and colors them with the same brush as the corporation they manage. Devoid of mutual trust, people use political processes to impose rigid conditions on corporate behavior. Managers respond in kind by satisfying the form of the law and legal requirements without concerning themselves with the substance or objectives for which those requirements were imposed. Where offending behavior is within acceptable norms of general business practice – whether or not it is illegal and punishable when found – its impact on the executive involved is limited and short-lived. Individuals do not see their unethical actions as causing great social harm when they form part of a large common pattern whose pervasive collective impact they all abhor. The unethical behavior of the CEO – conveniently defined as allegedly small variations from socio-ethical norms – is often judged leniently within the reference-peer group whose loyalty and support is more important than that of the public-at-large for legitimizing his/her self-worth and within group status.

For corporate managers to act beyond the minimally prescribed and legally enforced norms of social conduct, it would be important to foster mechanisms for generating a higher threshold level of trust between business leaders and leaders of other socio-political institutions on the one hand and business leaders and the public-at-large on the other hand. An important element of this approach would necessitate a redefinition of the nature of the “business game”, moving away from its predominantly zero-sum character of gains and losses in dealing with one or more elements of society. One of the ways to develop “cultural isomorphism” would be through conscious imitation and adaptation of *symbols of social success* that have worked well within and between the context of other social institutions. This would not necessarily call for a diminution of

competitive spirit. Instead, it would enforce those social conditions that would foster a more proactive corporate ethical behavior in the firm's dealings with other social institutions and individuals.

One of the important ways in which we might improve corporate ethical conduct and accountability would be to encourage in the CEOs a broader vision of their role – and those of the companies they manage – in society. This could be accomplished by elevating the corporate chief executive by endowing him/her with the stature of an important public figure. To this end, it is suggested that:

- (a) The selection of a CEO of a major corporation should be considered an important social decision requiring significant public discussion and exposure;
- (b) The installation of the CEO of a major corporation should be invested with great pomp and ceremony, i.e., investiture that such an office should command given the importance of that institution to the welfare of the nation. This would be akin to the investiture of the high office of the presidents of major universities and other important social and political institutions;
- (c) Such a selection process would not constitute a democratic process in the appointment of a CEO. Nor would it mean that a CEO so selected would necessarily be incompetent or unacceptable to the board of directors. However, by investing the job with a greater sense of social recognition, we would give the occupant a better self-image and encourage him/her to assume a broader perspective of his/her function and role at the helm of a major corporation;
- (d) At the time of assumption of office, the CEO would announce to the public what specific policies he/she would pursue to improve the quality of the company's

operation, its other stakeholders, the communities where the company has major operations, and society-at-large. The CEO would also make specific pledges that could be monitored through independent oversight – as to the norms of ethical conduct the company would apply in its operations and in dealing with its internal and external stakeholders;

- (e) There would be a systematic and regular process – akin to that currently applied to financial disclosures and reporting – for the companies to report on its activities not covered in its financial reports.

In theory, all corporations could follow this course. However, in reality, it is likely to be confined to the top 50-100 companies because of the public attention that such an activity must command in order to be meaningful. Over time, suitable traditions would develop. There is no reason to believe that these ceremonies would not be conducted with the same degree of restraint and dignity as those of the investiture of a university president.

We must not reject this exercise as mere frivolity and an attempt at self-aggrandizement and propaganda. Those who are constantly berated as unworthy tend to see the world in a similarly unfavorable light as they try to eliminate dissonance by coloring the world in the very image fostered upon them by society. The process in the end is self-defeating, as both the individual and the institution involved try to destroy each other. The sole purpose of this exercise would be to set a moral tone for the CEO and corporate management. Philosopher kings are not unknown in history. Philosopher scientists are commonplace today. Isn't it time that we asked for philosopher managers to run or major economic institutions? (Votaw and Sethi, 1973).

The arenas of social conflict between business and society are not those between right and wrong, or between guilty and innocent, but between one type of inequity and another, between giving one group more while taking some from another group, between the virtue of frugality and the sin of accumulation, and between morality of principle and morality of situations. In an unjust world, the distinctions between the guilty and innocent have become ambiguous. What we are confronted with is the realization that we live in an increasingly interdependent society where individual good is not possible outside the context to common good. It makes no sense to separate moral principles from institutional behavior, political power from material rewards. To do so is to divorce the social system from its basic element, the human being, who does not behave in a fragmented manner.

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